

A scenic landscape photograph of a mountain valley. In the foreground, a stone bridge with a single arch spans a small stream. The middle ground shows a cluster of traditional wooden houses with red roofs, some with solar panels, nestled in a lush green field. The background features rolling green hills and a range of rugged, rocky mountains under a blue sky with scattered white clouds. A flock of birds is visible in the upper left sky area.

Private Credit Primer

Part 1: Origin, Strategies, Players, and Bubbles

www.unityinvestments.com

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About Unity Investments

Our mission at Unity is simple yet profound: to create better access. Specifically, Unity identifies, catalyzes, and capitalizes on the most compelling alternative investment opportunities and shares them with our investors. In the long run, we aim to level the playing field.

Today, our investments business predominantly focuses on high-yielding private credit opportunities in the U.S. By building our origination network, underwriting team, and fund administration capabilities in-house, we control the entire investment process end-to-end to ensure quality and consistency. Selected for asymmetrical risk-reward and downside protection, our private credit deals are bespoke, privately negotiated, rigorously underwritten, and creatively structured. To learn more, please visit www.unityinvestments.com.



Contents

Opening Thoughts 4

1 What is Private Credit? 5

Definitions

Market Size

Broad Lending Categories & Sub-strategies

2 What Drove the Rapid Rise of Private Credit? 7

Basel III

Dodd-Frank

2013 Capital Rules

3 From Whom Did Private Credit Take Share? 10

The Corporate Credit Landscape

Lower-Middle Market

Deterioration of Regional Banks

4 Who Are the Major Players? 12

Assets Under Management

Collateral Type: Cash-Flow v. Asset-Based

5 Is Private Credit a Bubble? 14

GFC Comparison

Default Rates

Market Share

Areas of Concern

Closing Remarks 17

Opening Thoughts

Investors often ask us: “What is private credit?” While the term “private credit” is used ubiquitously, we realized that most investors have only a broad, hazy understanding of what private credit is. Many also assume uniformity across all private credit strategies.

In reality, private credit is a ~US\$2 trillion¹ global market, which has wide variations in loan structure, duration, collateral quality, and risk profile. We segment the private credit landscape into three practical buckets: (1) direct lending, (2) asset-backed/structured lending, and (3) opportunistic or special-situations lending.

To provide clarity and transparency, we have decided to embark on a journey to address the most important and foundational topics related to private credit through a four-part white paper series. In Part I, which provides an overview of the industry, we answer the following questions:

- **What is private credit, and what is its market size?**
- **What are the different types of private credit?**
- **Why did the industry grow so quickly?**
- **Who are the major players?**
- **Do we see any bubbles in the market or parts of the market?**

To put things in context, private credit has delivered consistent, high-yield returns for the better part of two decades. Its track record is still relatively young, having entered the spotlight only after 2008, when banks were subject to tighter global financial regulations.² For investors, private credit offers regular cash flow and high yields at a comparative premium to publicly traded fixed-income. In exchange for a higher yield, private credit is not tradeable in most instances.

Our overarching goal is to educate our investors and the broader investment community. Private credit is an exciting asset class, but it is not without its complexities. Our job is to parse through the industry jargon and technicalities and explain our insights in plain, understandable terms.

What is Private Credit?

What is Private Credit?

Private credit involves providing capital outside the traditional banking system, referred to as “non-bank lenders.” Specifically, non-bank private lenders originate and negotiate loans directly with borrowers. These loans are not traded on public exchanges, making the asset class illiquid. In return, the asset class generates higher yields and is governed by lighter regulatory oversight. For investors, it is a defensive allocation that offers customizable financing solutions and portfolio stability, as returns are less subject to macroeconomic volatility. For borrowers, it is access to flexible capital without the need to fit a bank’s rigid lending profiles or to issue equity and dilute shares.

As of the end of 2025, the total AUM in private credit is approximately US\$1.8 trillion and is forecasted to reach US\$2.3 trillion by 2028.¹ It comes as no surprise that private credit continues to grow and is now comparable in scale to public debt markets such as high-yield bonds or leveraged loans (see *Figure 1*).

Broad Lending Categories

There are generally six sub-strategies divided by the types of borrowers they lend to, the loans they make, or the collateral they require.¹ Even within the strategies, there are further branches. While we cannot discuss every strategy, it is important to note that private credit is not a uniform asset class. Each sub-strategy carries its own risk parameters, return profiles, and underwriting processes. At Unity, we like to categorize the different strategies into three broad-based categories - specifically: 1) direct lending, 2) asset lending, and 3) opportunistic credit.

Share of Private Credit AUM by Sub-strategy

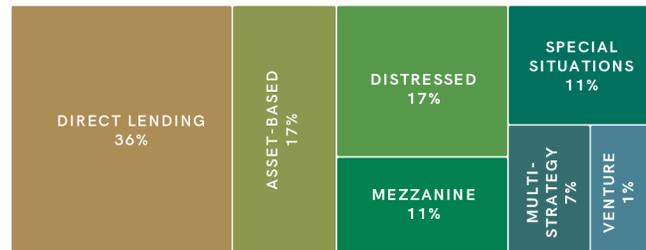


FIGURE 2. Data retrieved from Morgan Stanley Investment Management.¹

U.S. Corporate Credit Market by Size

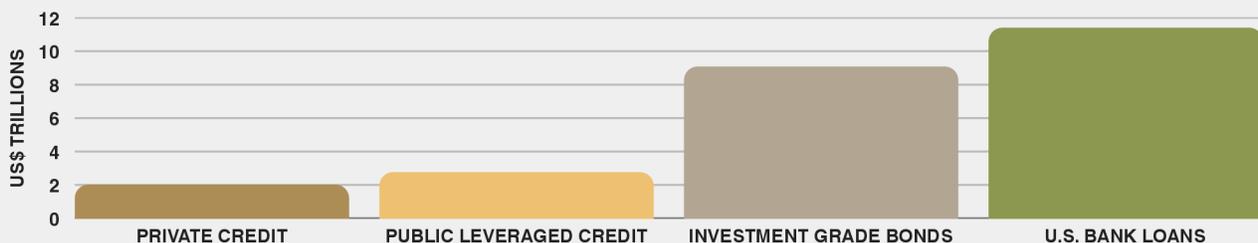


FIGURE 1. Data retrieved from Future Standard.³ Public leveraged credit consists of leverage loans (US\$1.40 trillion) and High-yield bonds (US\$1.36 trillion).

Sub-strategy Breakdown

DIRECT LENDING		DIRECT LENDING	Lenders originate and negotiate with borrowers without a third-party intermediary. Ranges in seniority and may be secured by collateral and covenants.
		MEZZANINE LENDING	Provides borrowers with a hybrid of debt and equity financing. Subordinated debt.
ASSET LENDING		ASSET-BASED LENDING	The lender extends funds secured by and dependent on the borrower's assets (accounts receivable, inventory, machinery/equipment, real estate), which remain as a part of the borrower's balance sheet.
		ASSET-BACKED FINANCE	Loans where assets are securitized often use a Bankruptcy-Remote Special Purpose Vehicle (SPV). The lender has a direct claim over the cash flows generated by the asset pool.
OPPORTUNISTIC CREDIT		SPECIAL SITUATIONS	Focuses on flexible solutions for events such as corporate expansion or restructuring.
		DISTRESSED DEBT	Lending to companies that are facing issues such as bankruptcy or complications with meeting debt obligations.
		VENTURE DEBT	Lending to startup / early-stage companies looking for funding.

TABLE 1. Data retrieved from Morgan Stanley Investment Management.¹



What Drove the Rapid Rise of Private Credit?

Key regulatory changes

The regulatory and market events that reshaped the financial system post-2008 contributed significantly to the rise of private credit. Driven by excessive leverage, weak underwriting practices, and lax regulatory oversight, the Global Financial Crisis (GFC) led to the collapse of major financial institutions while exposing systemic fragilities and deep incentive misalignments. In response, regulators worldwide implemented a series of reforms that constrained banks' capacity (and willingness) to extend credit, particularly to higher-risk borrowers.

Below, we discuss instrumental regulatory step-ups that aim to check financial institutions. This section is a bit more technical in nature; however, without understanding the regulatory changes in detail, it is hard to appreciate the capital vacuum that these regulations created.

Bank for International Settlements Framework III (Basel III)²

The Basel III accord significantly tightened requirements for banks. Institutions needed to maintain higher and more resilient capital buffers, ensure stronger liquidity positions, and adopt a more stable funding structure. Two key metrics, the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR), were enforced to safeguard the above sentiments.

i) LCR phased in starting 2015 at 60%, with a 10% annual step-up until reaching 100% by 2019. High-quality liquid assets (HQLA) are assets that can be easily converted into cash with minimal loss of value in the process (see *Appendix, Table 2*). Introducing LCR forces banks to hold larger liquidity buffers, reducing balance sheet flexibility and appetite for riskier lending as it requires greater HQLA stock.

ii) In 2021, major regulatory bodies globally implemented a threshold of NSFR $\geq 100\%$ over each one-year horizon. Available Standard Funding, or ASF, is a measure of the relative stability of an institution's funding sources, and the ASF factor represents the carrying value of an institution's liabilities for each source.

Required Stable Funding, or RSF, depicts the risk profile of their assets, where the RSF factor approximates the amount an asset is to be funded over the course of a year (see *Appendix, Table 3*).⁴

To maintain an NSFR $\geq 100\%$, the following must be true: ASF \geq RSF. An ASF factor of 100% is assigned to stable funding sources such as regulatory capital or instruments with residual maturity over a year. Sources with terms under a year, as well as those that have volatile deposits, decrease the ASF factor (see *Appendix, Table 3*).

Cash has a 0% RSF factor, meaning all cash held does not contribute to RSF. Non-performing loans have a 100% RSF factor, meaning the entire value of non-performing loans contributes to an increase in RSF. In times of stress, these assets become funding-intensive and require sources with higher ASF factors to offset the higher RSF (see *Appendix, Table 3*).

Effectively, introducing NSFR discourages banks from chasing illiquid, riskier assets that could potentially become non-performing loans.

Dodd-Frank Wall Street Reform and Consumer Protection Act⁵

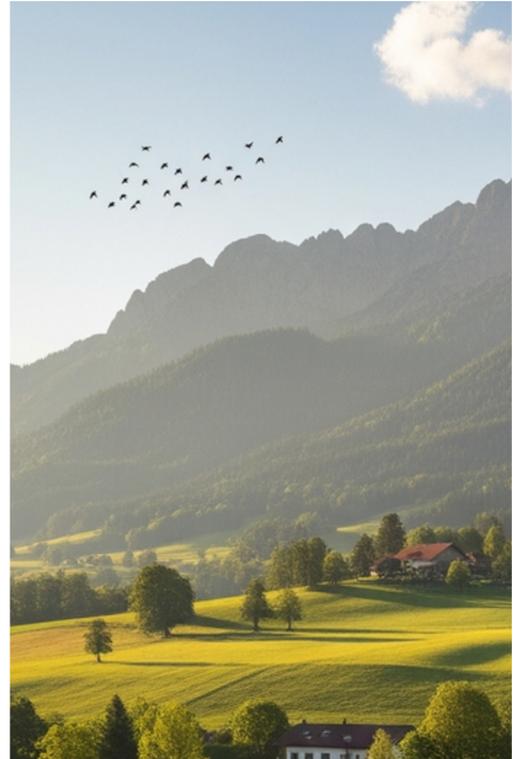
The Dodd-Frank Act of 2010 is legislation passed in the U.S. to overhaul the nation's financial system. Through financial stability oversight (Title I)⁵, failure management (Title II)⁵, stress tests & living wills (Title I Sec. 165)⁵, and the Volcker Rule (Title V, Sec. 619)⁵, Dodd-Frank fundamentally changed the risk behaviors and incentives of the U.S. financial industry.

Key Sections

Section 165: Any bank holding company (BHC) with \geq US\$50 billion in consolidated assets, triggered enhanced prudential standards in the form of stress tests (CCAR, DFAST) and resolution planning. The section also introduces a maximum debt-to-equity leverage ratio of 15:1.

Section 619: Explicitly, the Volcker Rule outright prohibits: 1) “engaging in proprietary trading”⁵ or 2) “acquiring or retaining any equity, partnership, or other ownership interest in or sponsoring a hedge fund or a private equity fund”⁵. This essentially barred banks from riskier investment vehicles.

Section 941 § 15G: Banks that securitize loans must keep at least 5% of credit risk. If the loan defaults, banks cannot hedge or transfer the risk to investors.



As a result, banks evolved to become more risk-averse. Although certain aspects of the Dodd-Frank Act were relaxed in 2018, which we will address below, the overall attitude and risk tolerance of banks remain significantly lower than they were pre-GFC.

Moreover, periodic reviews and revisions provide the necessary updates to the aforementioned metrics. In 2018, Congress passed the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCP Act)⁶, which set out to amend the Dodd-Frank Act, effectively raising the asset threshold of banks subject to annual stress testing from US\$50 billion to US\$250 billion.

The most recent update followed the collapse of Silicon Valley Bank (SVB) in 2023. The 2018 reforms exempted SVB from both LCR and NSFR requirements recommended in Basel III, because the bank was under the newly implemented asset threshold.⁷ However, after SVB collapsed, Congress introduced the Secure Viable Banking Act⁸ to repeal the EGRRCP Act and lower the asset threshold again, mainly to re-regulate smaller banks.



2013 Capital Rules⁹

Complementing these broad reforms, in 2013, the FDIC, Federal Reserve Board (FRB), and the Office of the Comptroller of the Currency (OCC) issued post-crisis regulations for U.S. institutions to align with Basel III standards. The 2013 Capital Rules established risk-weighting approaches by defining risk-weighted assets (RWA). It also promoted common equity tier 1 (CET1) capital, as it is the most loss-absorbing form of capital. This was achieved by increasing the Prompt Corrective Action (PCA) thresholds to capital-to-RWA ratios of 4.5%, 6%, and 8% for CET1, tier 1, and total (tier 1 + tier 2), respectively. Additionally, requirements to maintain a capital conservation buffer of $\geq 2.5\%$ were introduced.

Following the SVB collapse, the FDIC released a supervisory statement¹⁰, further emphasizing the importance of Contingency Funding Plans. Specifically, the FDIC advised regularly testing for access to funding sources, operational readiness for contingency collateral, and maintaining a connection with the Federal Reserve to strengthen resilience in adverse conditions.

Collectively, these regulatory changes restricted banks' balance sheet flexibility and limited their ability to make risky loans. The overall shift away from aggressive lending practices narrowed the scope of bank activity. This created a funding vacuum, thus providing room for alternative lenders, notably private credit funds, to grow.

3

From Whom Did Private Credit Take Share?

Bank Lending & Public Bonds

Historically, corporate borrowers have looked to banks and/or the public bond market to meet their financing needs. For reference, in 2007, on the eve of the GFC, outstanding commercial and industrial (C&I) loans from U.S. banks were US\$1,417 billion¹¹, public corporate bond issuance US\$889 billion¹², and private credit was a marginal afterthought. Since then, however, the corporate credit landscape has shifted dramatically (see *Figure 3*). In July 2025, outstanding C&I Loans in July 2025 were US\$2,870 billion¹¹, corporate bond issuance LTM was US\$2,036 billion¹³, and private credit is now a US\$1,800 billion¹ industry. As we can see from the chart below, private credit has taken the largest amount of market share from banks. Moreover, private credit has also expanded the corporate credit market at large by providing a high degree of customization, flexibility, and stability.

Market Share: C&I v Corporate Bond Issuance v Private Credit

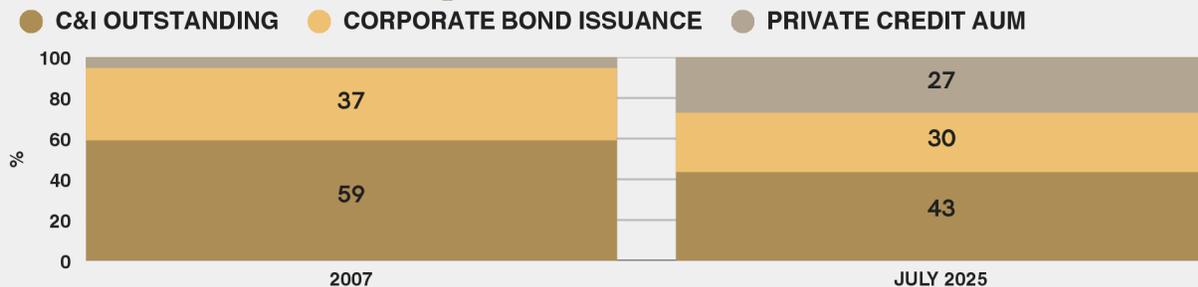


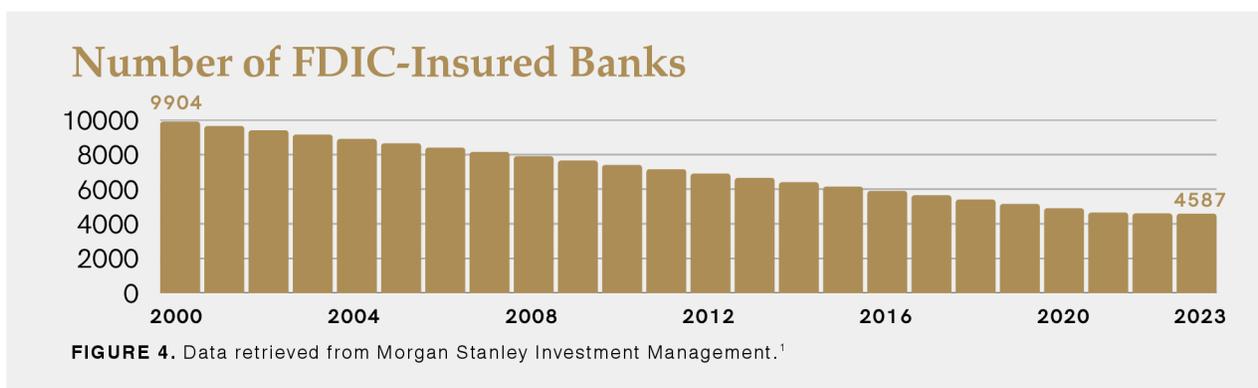
FIGURE 3. Data retrieved from Multiple Sources.^{1,11,12,13,14}



A note on lower middle market, banks & SVB

Of the 18 million companies in the U.S., only ~37,000 generate annual revenues greater than US\$100 million.²⁴ In other words, 99.8% of businesses are classified as small to mid-sized businesses (defined by Figure 5). The sheer size of the market makes the lower-middle market private credit particularly attractive. The decline of regional banks partially contributed to this dynamic.

Specifically, the number of FDIC-insured US banks has declined by 53% between 2000 and 2023, falling from 9,904 to 4,587 institutions (see Figure 4).¹ Much of this consolidation occurred in the years immediately after 2008, when smaller banks, especially those reliant on real estate loans, were acquired by larger/healthier institutions. The result was a reduction in credit availability, especially for small/middle-market businesses.



In 2023, the deterioration of regional banks culminated in the collapse of SVB. As a last-resort lender to many startups, SVB experienced rapid deposit withdrawals and losses on long-dated securities in a rising interest rate environment. This exposed the vulnerabilities of mid-sized lenders, as the FDIC had to broker numerous regional bank sales in the aftermath of the SVB collapse.²⁶ As regional banks stepped away, private lenders stepped in. This shift is the most significant in the small/middle-market, which generates US\$29 trillion^{1,15} in annual revenue (see Figure 5). Even now, from our daily conversations with our borrowers, we see the entire lower-middle market as underserved and under-banked.



4

Who are the Major Players?

The most prominent private credit players are Apollo, Blackstone, KKR, Ares, and Carlyle. We know that different sources cite different major players, but regardless of the ranking, most of the top credit players are also private equity sponsors. Because most private equity deals—especially large buyouts—require leverage, the transition from private equity to private credit was very natural. Historically, sponsors mainly relied on syndicated bank loans and/or the public bond market. That preference has steadily and resolutely migrated to private credit over the past decade.

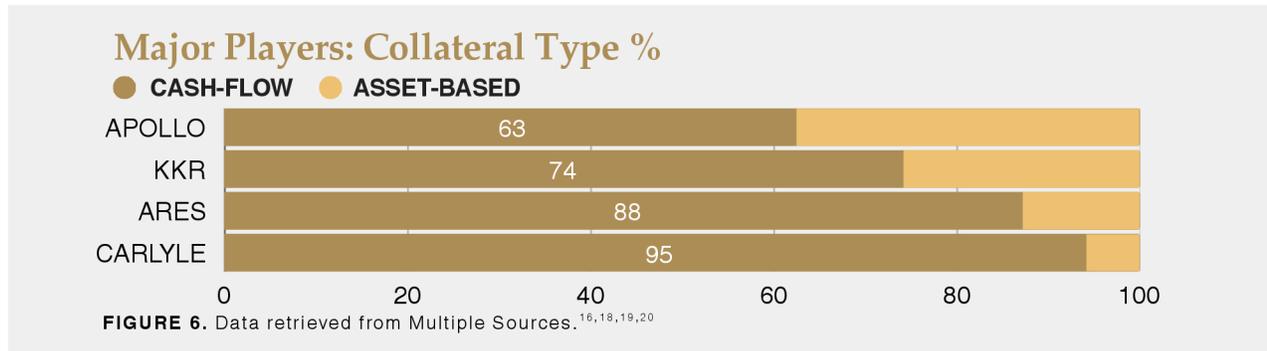
Below is a table summarizing the credit AUM of major players, as well as their undeployed dry power. We can see a clear evolution of their private sector focus, as more capital is diverted from private equity into private credit strategies.

Major Players <i>(as of Q2 2025), in US\$bn, unless otherwise stated</i>	Credit AUM	% of Total AUM	YoY Growth	Dry Powder
APOLLO	\$690	82%	23%	\$42
Blackstone	\$407	34%	23%	\$48
ARES	\$377	66%	17%	\$103
KKR	\$292	43%	10%	\$26
CARLYLE	\$203	44%	7%	\$17

TABLE 4. Data retrieved from Multiple Sources.^{16,17,18,19,20}

Collateral Type: Cash Flow v. Asset-Based

A closer look at top players' credit strategies suggests that lending against cash flows is still preferred over asset-based finance (see *Figure 6*). This could be partially due to the size of said institutions and the availability of quality, pledgeable assets. At the same time, deals backed by private equity sponsors prefer loans secured by cash flows.



While there is nothing wrong with cashflow lending, the nature of cashflow lending makes it more sensitive to macroeconomic factors, monetary and fiscal policy changes, and liquidity conditions. At the same time, large, cashflow-rich businesses typically do not have a shortage of funding options from the public market (both equities and debt) to bank loans. As a result, the spread for cashflow lending can be quite tight.



Is Private Credit a Bubble?

To answer this question, we need to define what a “bubble” is. In equities, a bubble is usually associated with excess, speculation, and a detachment from fundamental value. In the world of credit, a bubble exhibits itself slightly differently than the equities world. A bubble appears when the interest rate or spread (usually over the risk-free rate) is too low to compensate for the risk of principal loss. Typically, excess capital and liquidity moving into an asset class rapidly result in lax underwriting and irresponsible deployment. The extraordinary growth of private credit over the past decade in size, scope, and breadth has led to concerns about a bubble.



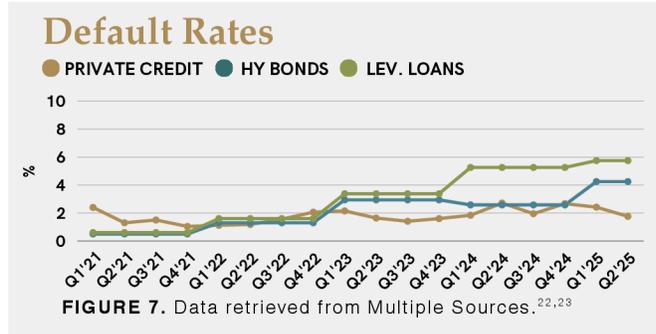
GFC Comparison

To understand where we are in a cycle, we will look at three important indicators: 1) private sector debt to GDP, 2) real estate asset prices, and 3) high-yield credit default rates. On the eve of the GFC, as compared to 2000, private sector debt to GDP rose from 135% to 171%²⁹, real estate prices increased by ~70%²¹, peaking in 2006, and credit default rates went from 2% in 2000 to ~13% in 2008. The bubble then deflated through a painful deleveraging process, as asset prices and default rates normalized over time.

In comparison, from 2012 to 2023, a period when the U.S. private credit industry quadrupled, the total private sector debt to GDP increased from 155% to just 156%, with an ephemeral rise in 2020 coinciding with the COVID Paycheck Protection Program (PPP) spike.²¹ Real estate prices, however, did rise by 104%³¹, primarily driven by a post-COVID jump. High-yield default rates are slightly elevated at 4-5%, but still low as compared to the GFC, where default rates for high-yield bonds and leveraged loans peaked at 13%²⁷ and 11%²⁸, respectively.

Private Credit Default Rates

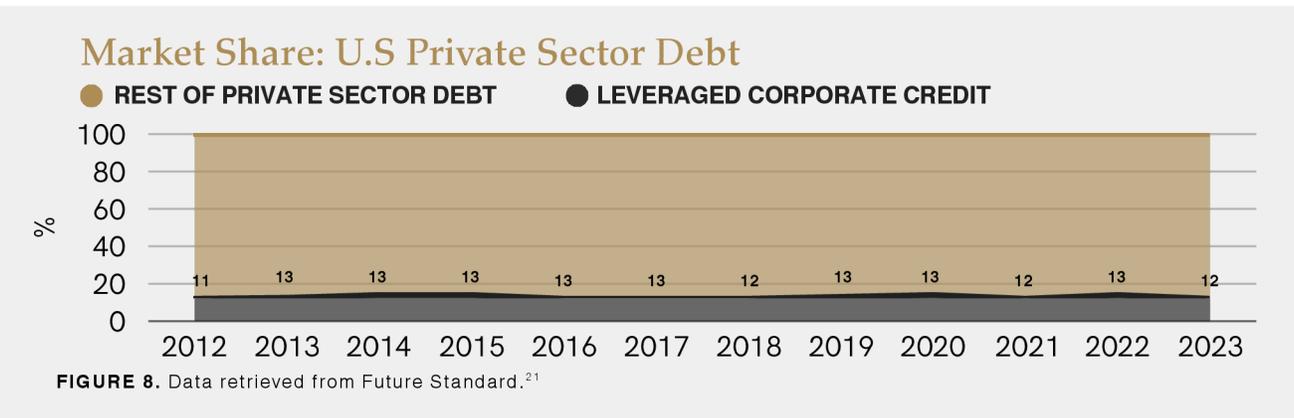
As of 2025, the default rate for private credit sits at 1.76%²² for the industry. This is low even compared to those of high-yield bonds at 4.25%²³ and leveraged loans at 5.75%²³. It is also low compared to history, where between 2004 and 2024, high-yield bonds and leveraged loans had an average annual default rate of 2.45% and 4.27% respectively.²⁴ Private credit's low default rate can be attributed to its 1) relative dissociation from macroeconomic volatility and 2) strong underwriting standards historically. It can also speak to where we are in the macro cycle. To this point, *Figure 7* highlights that while high-yield bonds and leveraged loans' default rates have picked up slightly since Q4 2022, the default rate for private credit has remained low.



While performance across different funds can vary significantly, the industry-level data is encouraging. We also believe that as the Fed begins to cut rates, credit quality across the board should improve and default rates across all credit should recede in the coming quarters.

Market Share

From our perspective, private credit's growth is more of an asset reallocation within the credit market than a move into a whole new sphere of capital provision. For example, *Figure 8* shows that leveraged corporate credit (which includes private credit, HY bonds, leveraged loans, and commercial bank loans) has remained a consistent proportion of the rest of private sector debt. This is despite private credit growing from US\$108 billion¹⁴ in 2007 to US\$1.8 trillion¹ today. In other words, investors have restructured their portfolio to increase private credit assets by reducing their exposure to other leveraged corporate credit. Based on the current context and historical comparables, we do not observe conditions consistent with a broad-based bubble in private credit at this time.



Areas of Concern

However, we do have three potential areas of concern on the hidden risks within the private credit industry.

Incentive alignment

First, we do not know how incentives will be aligned if the Sponsor finances both the debt and the equity side of a deal. If the credit side needs to enforce on the loan—thus putting the equity piece at risk—how will the Sponsor balance its interest? Can the credit side stay independent and truly act as a fiduciary for its LPs, despite hurting the broader interest of the Sponsor?

Back leverage

Second, almost every large credit fund uses back leverage to boost its returns. Back leverage is when a credit fund borrows money at the fund level (not at the portfolio company level) to finance part of its portfolio of loans or credit investments. However, given that default rates are so low in private credit, funds are emboldened to take on more leverage. While we currently do not use leverage as a strategy to enhance our returns, it is common practice in the industry. When default rates do inevitably rise, can private credit funds still sustain their stable returns?

Deployment pressure

Third, there has been a substantial inflow into private credit, especially into first-lien direct lending. Among just the top five players, there is ~US\$236 billion^{16,17,18,19,20} in uninvested dry powder (see *Table 4*). This dynamic might force some funds to relax their underwriting, collateralization, and covenant requirements merely to deploy excess capital. Thus, what happens if funds are “forced” to deploy because of competition and top-down mandates?



Lastly, Rudi Dornbusch, a renowned German-American Economist, famously said: “A crisis takes a much longer time coming than you think, and then it happens much faster than you would have thought.” By identifying potential canaries, we want to prepare for black swan events long before they happen.

Closing Remarks

Over the past decade, private credit has evolved from a niche to a core strategy in capital lending, growing in response to tighter banking regulations and the resulting market dislocations. However, the industry's pace of expansion has also raised questions about performance sustainability.

While we do not see a large credit market dislocation, we are tracking all the factors that could contribute to the market's overheating and aim to adjust our risk parameters in real time. For example, because default rate is a lagging indicator, we also monitor certain co-indicators—from non-accrual/watch list loans (similar to delinquency rate) to covenant-lite loan issuances (a proxy for industry underwriting rigor)—closely to keep a pulse on the broad credit market.

Longer term, with rising global trade fragmentation, production frictionalization, geopolitical tension, and domestic labor cost, we will likely remain in a secularly higher rates environment. Therefore, private credit—especially asset-backed lending, in our opinion—should be able to provide superior risk-adjusted returns for years to come.

For the coming weeks, we will continue our series with a deep dive into each of the three sub-strategies of private credit. In the meantime, if you would like to learn more about how we approach private credit and related topics, please feel free to reach out to us at IR@unityinvestments.com.

This is Life, Compounded. $A = P \left(1 + \frac{r}{n}\right)^{nt}$



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Appendix

LCR = HQLA Stock / Total Net Cash Outflows over 30 days		
Net Cash Outflow = Outflows - min(Inflows, 75% of Outflows), 75% cap to prevent over reliance on payments		
HQLA Level	Asset	Haircut / Cap
1	<ul style="list-style-type: none"> • Coins and bank notes • Qualifying marketable securities from sovereigns, central banks, PSEs, and multilateral development banks 	No haircut / No cap
2A	<ul style="list-style-type: none"> • Sovereign, central bank, multilateral development banks, and PSE assets qualifying for 20% risk weighting • Qualifying corporate debt securities & bonds rated AA- or higher 	15% / 40%
2B	<ul style="list-style-type: none"> • Qualifying RMBS & common equity shares • Qualifying corporate debt securities rated between A+ and BBB- 	25~50% / 15%

TABLE 2. Data retrieved from BIS.² Equations for LCR, Net cash outflows. Table of HQLA levels (Not a complete list).

NSFR = ASF / RSF	
ASF = [∑Liability Category Value × ASF Factor], RSF = [∑Liability Category Value × RSF Factor]	
Liability Type	ASF Factors
• Total regulatory capital (excluding Tier 2 instruments with residual maturity of less than one year)	100%
• Stable non-maturity (demand) deposits and term deposits with residual maturity of less than one year provided by retail and small business customers	90-95%
• Funding with residual maturity of less than one year provided by non-financial corporate customers	50%
• All other liabilities and equity not included in the above categories, including liabilities without a stated maturity (with a specific treatment for deferred tax liabilities and minority interests)	0%
Asset Type	RSF Factors
<ul style="list-style-type: none"> • Coins and banknotes • All central bank reserves 	0%
• Unencumbered Level 1 assets, excluding coins, banknotes and central bank reserves	5%
<ul style="list-style-type: none"> • Unencumbered Level 2B assets • HQLA encumbered for a period of six months or more and less than one year 	50%
• Unencumbered residential mortgages with a residual maturity of one year or more and with a risk weight of less than or equal to 35% under the Standardised Approach	60%
• Cash, securities or other assets posted as initial margin for derivative contracts and cash or other assets provided to contribute to the default fund of a CCP	85%
<ul style="list-style-type: none"> • All assets that are encumbered for a period of one year or more • NSFR derivative assets net of NSFR derivative liabilities 	100%

TABLE 3. Data retrieved from BIS.⁴ ASF & RSF Factors (Not a complete list).



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