

Private Credit Investing in Volatile Times

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Capital markets have experienced heightened volatility after President Trump announced a new tariff regime in April. Valuations for public stocks and bonds have fluctuated widely as participants assess the direct impact of ongoing trade negotiations on specific sectors and businesses. With that in mind, what are the implications for private credit? Let's start with an overview of credit markets, tariffs, and the early signals of economic strain.

Like the rest of capital markets, trade policy uncertainty is dominating investor sentiment in credit markets. The sweeping expansion of tariffs—impacting nearly every major US trading partner—has not only disrupted global supply chains, but also introduced a powerful new variable into business planning, earnings forecasts, and household behavior. As these policies take hold, early signs of strain are emerging across the economy.

The corporate sector is reacting quickly. Inventories had already begun to rise in anticipation of tariff-related disruptions. With order volumes falling and capital expenditures declining, many firms are reassessing their growth plans. Earnings expectations are being challenged in response to rising input costs and softer demand.

KEY TAKEAWAYS

- ➔ While not immune to the shifts in policy and the macroeconomic outlook, we expect to see resilient demand for private credit as the need for direct, larger, and more flexible financing remains and is likely reinforced by economic uncertainty.
- ➔ The leveraged credit market primarily finances domestic companies focused on sectors that are less directly impacted by tariffs—giving investors a chance to build portfolios that can better withstand periods of lower economic activity.
- ➔ Sharp focus on senior secured, first-lien debt is always important but paramount in the current environment. Downside risks to the US economy mean increased cash-flow pressure and liquidity constraints across many segments of the market.
- ➔ Historically, private credit has shown resilience in times of market stress and provided relative downside protection with low correlation to other major asset classes. A focus on lending to large corporates can add another layer of protection, financing businesses with stronger cash flows, diversified earnings streams and well-established business models.
- ➔ Our work highlights a modern approach to core-plus allocations, showing that the addition of private credit to a portfolio of public fixed-income securities can enhance risk-adjusted returns.

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Perhaps most tellingly, CEO confidence—a leading indicator of corporate activity—has dropped sharply in recent months (**Exhibit 1**).

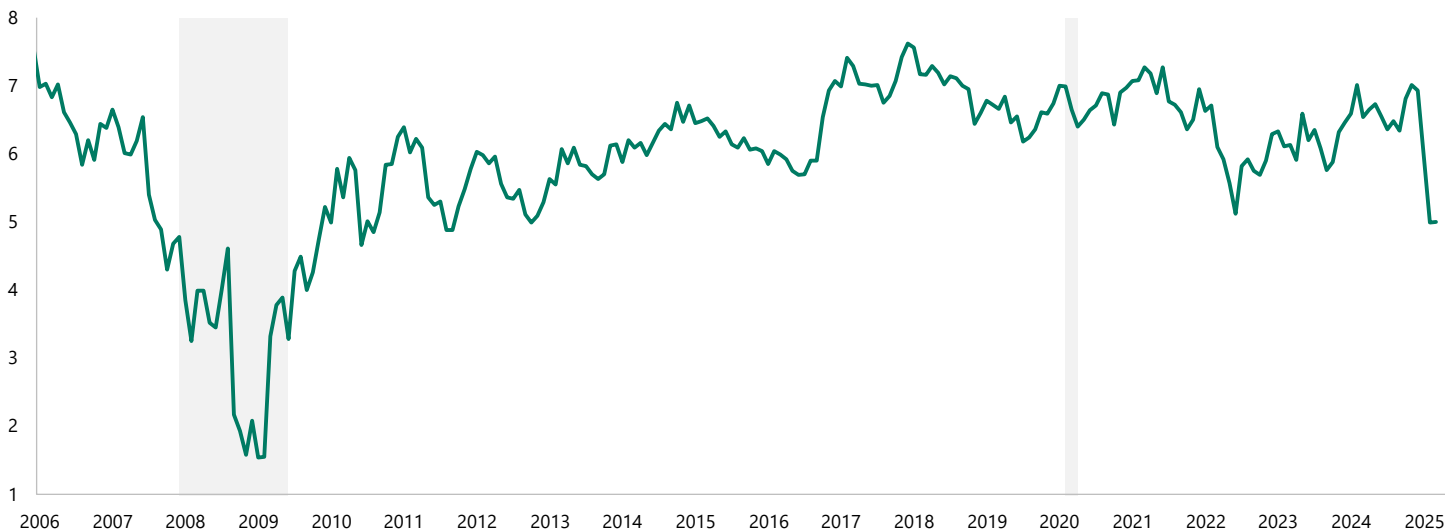
Households are reacting to uncertainty as well. While it has since recovered, consumer sentiment plunged in March (**Exhibit 2**), with many Americans having front-loaded large purchases in anticipation of higher prices. Meanwhile, international tourism to the US is showing signs of slowing—

both a reflection of weaker global demand and a signal that higher costs and policy friction are weighing on discretionary spending.

While it’s still early, these developments point to more than just a temporary adjustment. Tariffs are not only reshaping trade flows—they’re injecting volatility into the foundational pillars of growth: business investment, corporate earnings, and consumer demand.

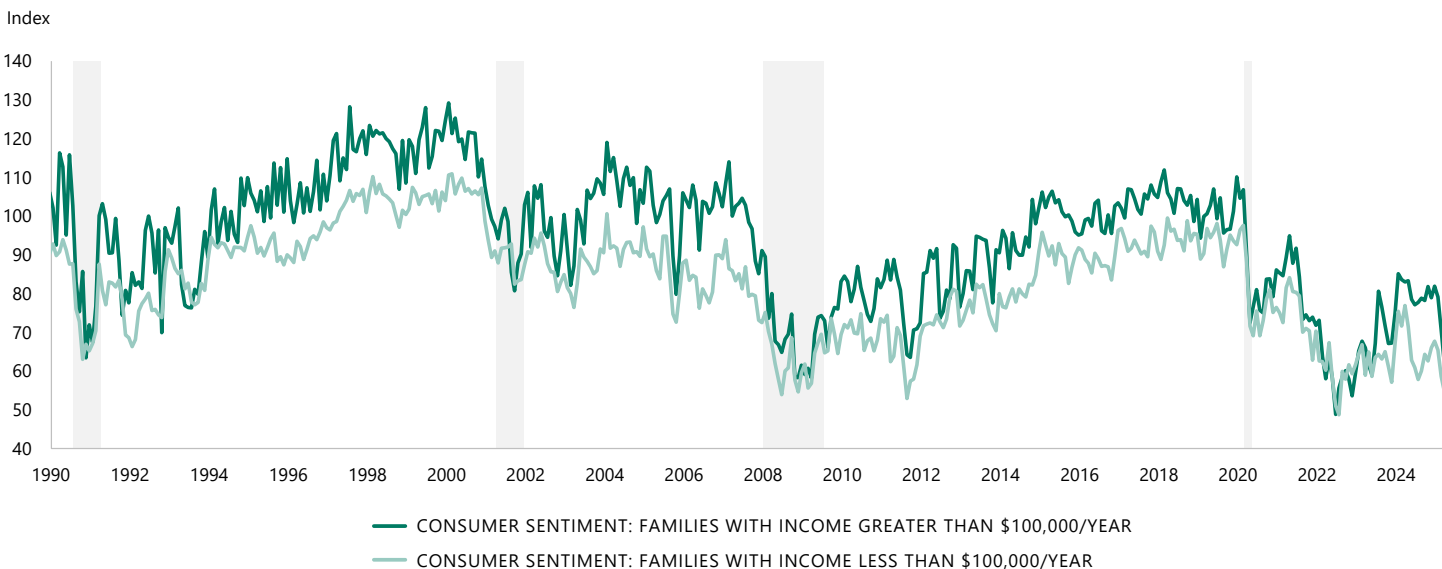
Exhibit 1: Business sentiment is deteriorating

CEO Confidence Index: Confidence in the economy 1 year from now



Data as of April 2025.
Sources: Chief Executive Magazine, Bloomberg, Macrobond, Apollo Chief Economist

Exhibit 2: Consumers are expecting harder times ahead



Data as of March 2025.
Sources: University of Michigan, Haver Analytics, Apollo Chief Economist

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Against this backdrop, spreads have widened in recent months. As **Exhibit 3** shows, the spread between CCC rated loans and B rated loans has expanded, suggesting that investors are becoming more concerned about potentially deteriorating fundamentals among the riskiest borrowers. Looking ahead, we expect volatility to persist and pressure on borrowers to intensify, particularly if declining sentiment gives way to weaker economic data.

Dissecting the Industry Impact of Tariffs

While the broader economic effects of tariffs are still emerging, certain industries are clearly more exposed than others (**Exhibit 4**). Industries with high global supply chain

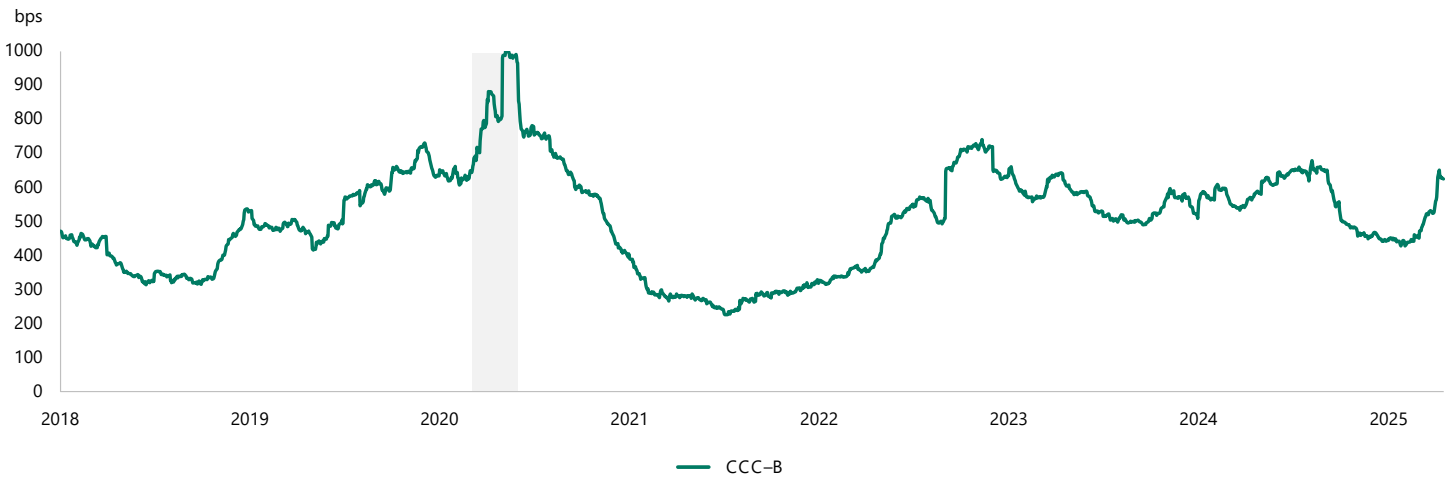
integration—such as retail, autos, and energy—face the most direct pressure, given their reliance on imported components and cross-border demand. By contrast, more domestically oriented sectors, including services companies and utilities, are expected to be less affected in the near term.

Compared to other credit markets, the leveraged loan space can exhibit a higher degree of insulation from the impact of tariffs, as corporate borrowers tend to have less direct exposure to international trade flow.

However, that does not mean they are immune. Second-order tariff effects—such as weakening consumer demand and margin compression—could pose challenges.

Exhibit 3: The spread between CCC and single-B has widened

US spread differential, CCC rated bonds minus B rated bonds



Data as of April 15, 2025.
Sources: Bloomberg, ICE BofA, Apollo Chief Economist

Exhibit 4: Industry impact of tariffs



Sources: Bloomberg, Apollo Chief Economist

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As economic growth slows and consumer behavior weakens, demand-side pressures can cascade across sectors, regardless of whether they were directly targeted by tariffs. Smaller issuers with limited pricing power and tighter liquidity are particularly at risk in this environment.

In our view, this sets the stage for a more selective credit environment—one where scale, flexibility, and balance sheet strength become increasingly important.

The US versus Europe: Changing Growth Dynamics

From a relative value perspective, one of the most important factors in 2025 is the evolving growth dynamics between the United States and Europe. For much of the last decade,

the US has served as the engine of global growth, driven by accommodative policies and strong consumer demand. Entering 2025, many of these supportive US policies have been unwound, while Europe has introduced stimulus initiatives aimed at boosting corporate investment (**Exhibit 5**). This shift is shaping how we think about relative value across regions, as the growth backdrop may now favor Europe over the US.

Larger Borrowers Are Better Positioned

Larger corporate borrowers have consistently demonstrated stronger fundamentals and greater resilience compared to smaller issuers—and in the current environment, those advantages are only becoming more pronounced.

Exhibit 5: Europe's pro-growth policy reversal

“ Merz Reaches Deal With Greens on German Spending Package ”

“ Germany's Defense Splurge Set to Favor European Companies ”

“ Germany is back ”

“ Germany is planning a massive defense-spending splurge, with a focus on European-made gear ”

Source: Bloomberg

Due in part to structural protections, private credit has historically weathered market downturns better than other parts of the credit spectrum.

As shown in **Exhibit 6**, large-cap companies continue to command healthy spreads while exhibiting stronger EBITDA growth than their smaller counterparts. Large borrowers can offer attractive risk-adjusted return potential, and they are growing earnings at a meaningfully higher rate than their smaller-cap peers.

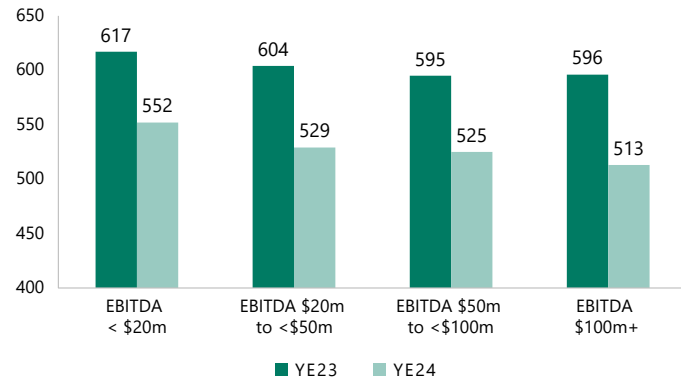
By contrast, smaller companies are encountering mounting challenges—many of which stem from persistently elevated base rates (**Exhibit 7**). Smaller firms are disproportionately

impacted by higher borrowing costs, which divert cash flow away from areas that would otherwise support business health and growth—such as inventory management, capital expenditures, and strategic investment. Instead, a growing share of operating cash flow is allocated toward interest expense.

The higher-for-longer rate environment is an increasing strain on smaller borrowers—especially those with thinner margins and limited balance sheet flexibility.

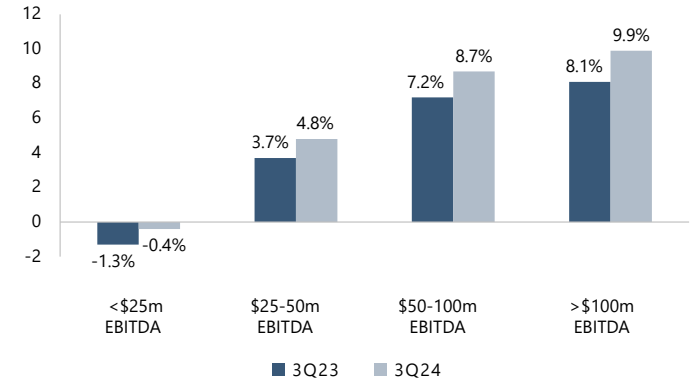
Exhibit 6: The risk return in private credit tends to favor large corporates

Spread of Direct Lending New Originations (bps)



Small Companies Only Provide Limited Addition Margin of 20-40bps

LTM EBITDA (YoY) (%)



Larger Companies Exhibiting Stronger EBITDA Growth

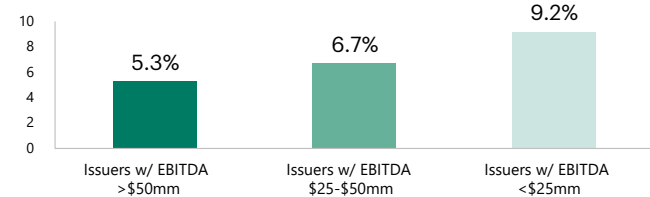
Sources (left): Lincoln International, Morgan Stanley Research (Q424 Private Credit Tracker).

Source (right): KBRA DLD Research; averages are based on a 3-month rolling basis. Annual recurring revenue deals are excluded.

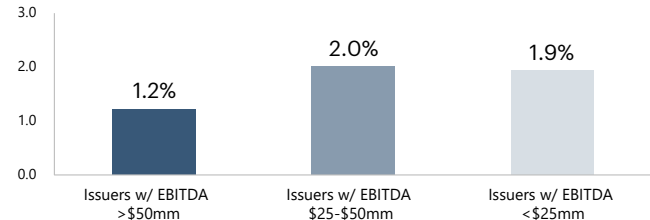
Exhibit 7: “Higher-for-longer” rates are impacting smaller issuers more severely

Private credit has been synonymous with middle market lending, which has exhibited a higher default rate

Q2 2020 DEFAULT RATE (PRIVATE CREDIT MARKET) (%)



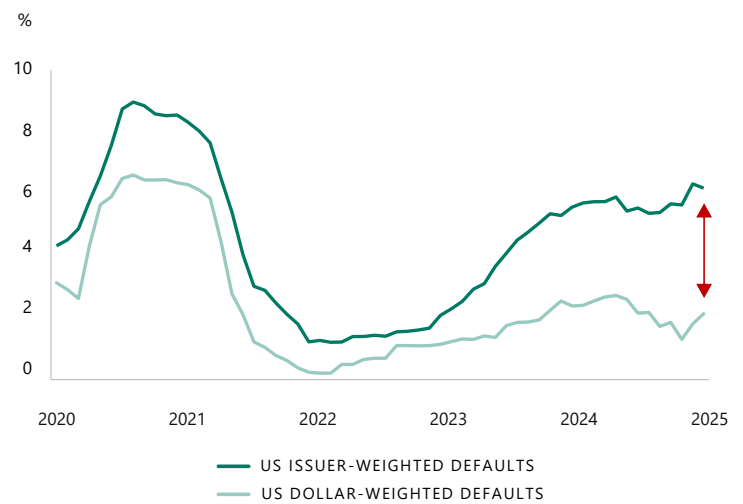
2021-2024 AVERAGE DEFAULT RATE (PRIVATE CREDIT MARKET) (%)



Source (left): Proskauer Private Credit Default Index as of December 31, 2024.

Source (right): Moody’s. Shows default rates for speculative-grade corporates.

Dollar-weighted defaults have recently been less severe, suggesting large companies tend to better navigate the higher rate environment



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In this context, the elevated rate environment becomes a structural drag for smaller issuers, potentially suppressing reinvestment, weakening credit metrics, and heightening the risk of distress.

As the outlook for monetary policy remains uncertain, we believe the downside risks are increasingly skewed toward these smaller-cap companies, which are less equipped to absorb sustained rate pressure. The result is a widening gap in default expectations—reinforcing the importance of credit selection.

In a more uncertain credit market, we continue to believe large-cap borrowers with the balance sheet strength, pricing power, and operational flexibility to weather uncertainty and deliver durable cash flow.

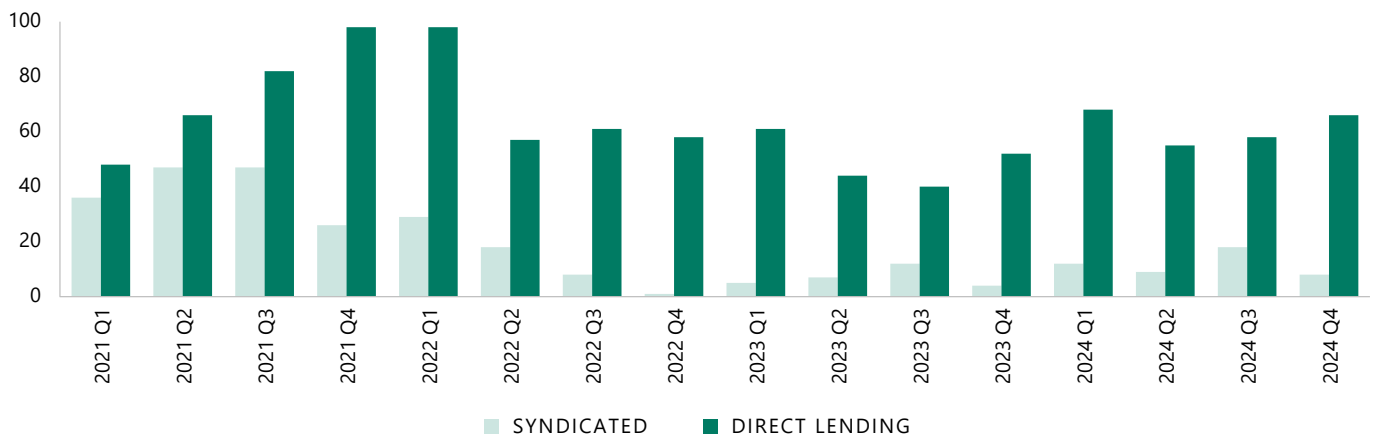
Demand for Private Credit Remains Strong

As shown in **Exhibit 8**, direct lending has emerged as the dominant source of financing for new LBO transactions, steadily overtaking the role traditionally played by syndicated loans. While deal volumes have moderated overall, private lenders continue to command a significantly larger share of the market—reflecting borrower preference for agility, confidentiality, and bespoke terms.

Private credit is not just a solution for new capital—it’s also playing a key role in refinancing existing debt. As illustrated in **Exhibit 9**, direct lending has become a meaningful source of capital for borrowers originally financed in the broadly syndicated loan (BSL) market. This refinancing activity underscores the increasing permeability between public and private markets—and further solidifies private credit’s role as a core financing engine for corporate America.

Exhibit 8: Direct lending has been the driver of financing for new LBO deals

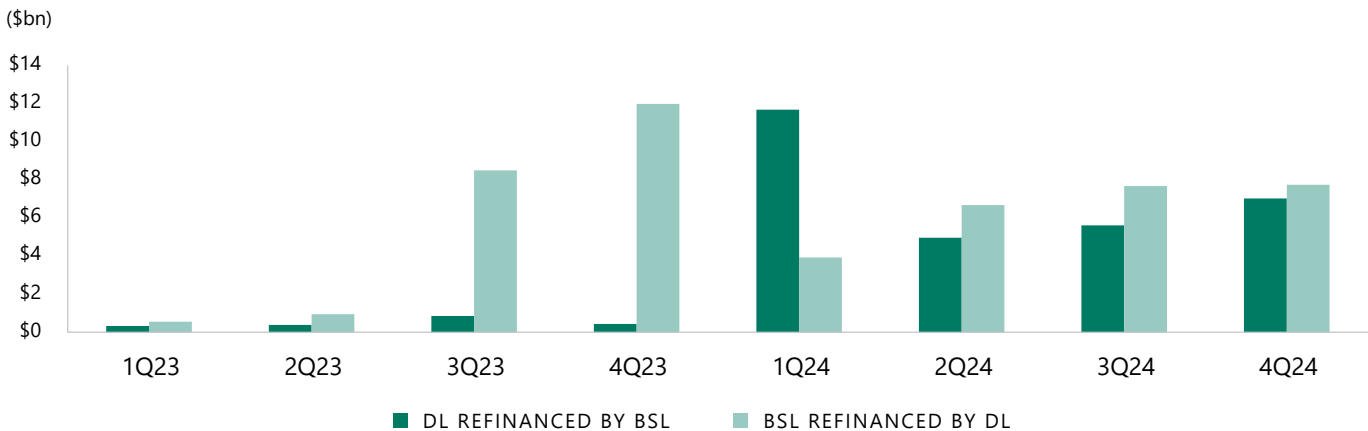
Number of transactions



Data as of December 31, 2024. Private credit count is based on transactions covered by LCD News. Reflects the views and opinions of Apollo Analysts and is subject to change at any time without notice. There can be no assurance that historical trends will continue. Sources: PitchBook LCD, Apollo Chief Economist

Exhibit 9: Direct lending strong source of refinancing activity

BSL / DL refinancings on par in 2024



Data as of December 31, 2024. Private credit count is based on transactions covered by LCD News. Sources: PitchBook LCD, Apollo Chief Economist

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For perspective, direct lending market share has grown over 7x in the past decade to 17% of the leveraged finance market.¹ Looking ahead, investors are likely to focus on the next sub-investment grade maturity wall, with more than \$620 billion in high yield bonds and loans coming due in 2026 and 2027.² This presents a substantial opportunity for private credit to extend its momentum as a key source of refinancing capital for companies facing upcoming debt obligations.

Private Credit Market Still Has Room to Grow

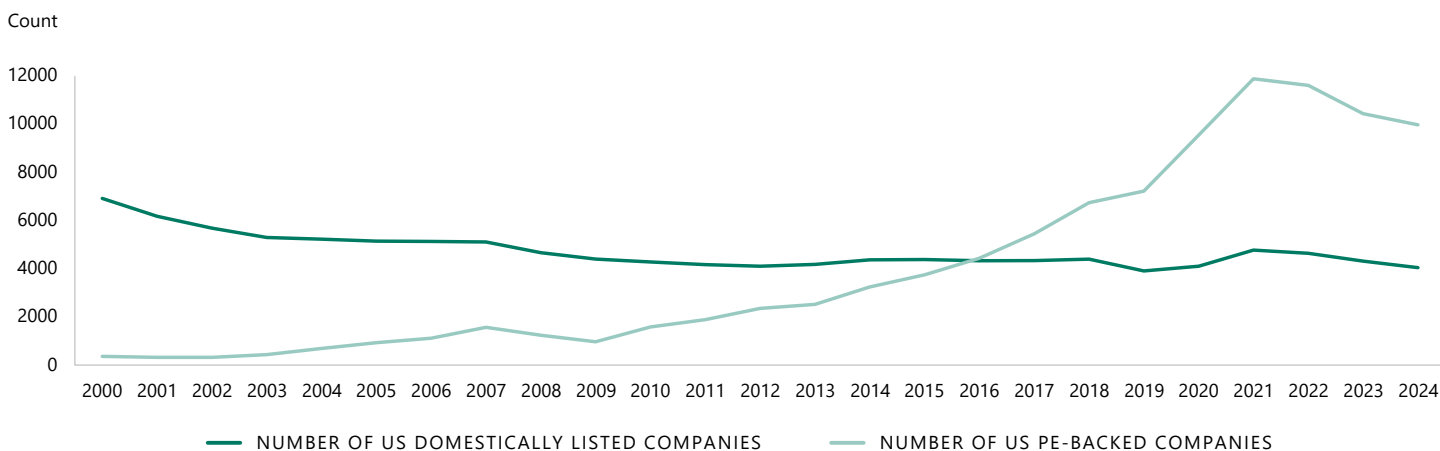
Has private credit gotten too big? It's a fair question, and one we hear often. The answer, in our view, is no—and the data supports that position.

The expansion of the private credit market reflects a broader structural trend: the shift from public to private financing. Over the past two decades, the number of publicly listed

companies in the US has declined significantly, while the number of private equity-backed companies has surged (**Exhibit 10**)—highlighting the growing preference among businesses to operate outside of the public markets.

From a borrower's perspective, private credit capital can offer attractive advantages over public debt markets. Private lenders are not bound by the same syndication process, or rigid documentation requirements that often slow broadly syndicated deals. Instead, they can provide speed, flexibility, and discretion—attributes that are especially valuable when companies are facing tight deadlines, navigating strategic transactions, or require customized terms. These benefits become even more critical in times of macroeconomic uncertainty, when public market access may be unreliable or unattractive.

Exhibit 10: The rise of PE-backed companies mirrors the decline of publicly listed companies



Sources: World Federation of Exchanges, World Bank, PitchBook, Haver Analytics, Apollo Chief Economist

Direct lending market share has grown over 7x in the past decade to 17% of the leveraged finance market.

¹ As of December 2024. Sources: Preqin, Bank of America Global High Yield Index, S&P Global Leveraged Loan Index

² Sources: JPMorgan, Bloomberg, S&P/IHS Markit

Importantly, and has been noted in this paper, private credit has evolved far beyond traditional middle-market lending. As shown in **Exhibit 11**, growth has been especially strong among large-cap borrowers, where private credit platforms can offer financing solutions such as delayed draw term loans, hybrid structures, and asset-backed facilities. This reflects a key shift: private credit is no longer an alternative; it is a mainstream financing solution for companies of all sizes.

Trends to Monitor: The Growing Prevalence of PIK

As private credit evolves to meet more complex borrower needs, one area drawing increased attention is the rise of Payment-in-Kind (PIK) structures. While PIK can offer benefits for both borrowers and lenders, it also introduces risk—especially in periods of economic uncertainty.

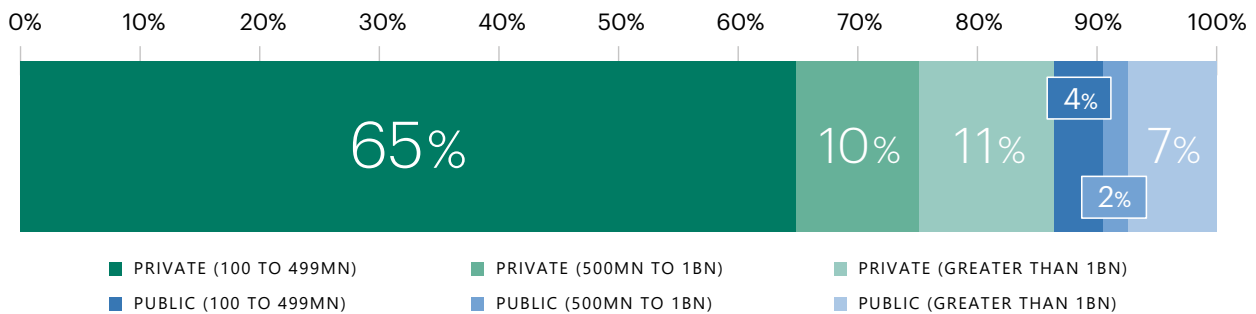
PIK allows borrowers to defer cash interest payments by adding them to the loan’s principal (**Exhibit 12**).

For example, instead of paying a 10% coupon in cash, the borrower accrues that interest to the outstanding loan balance. This results in a higher principal amount—and eventually, a larger repayment obligation.

From a lender’s perspective, not all PIK is created equal (**Exhibit 13**). Used prudently, it’s a tool for structuring flexibility and return enhancement. Used aggressively, it can mask borrower weakness and erode underwriting discipline. For example, PIK at origination can offer clarity and discipline, while partial PIK can provide incremental return potential alongside a higher principal. These structures can allow investors to benefit from a higher nominal yield than traditional cash-pay loans. On the flip side, synthetic PIK, where a borrower uses another form of debt to cover interest, compounds leverage and increases risk. Restructured PIK, the riskiest form, is often a red flag—signaling distress and potential default down the line.

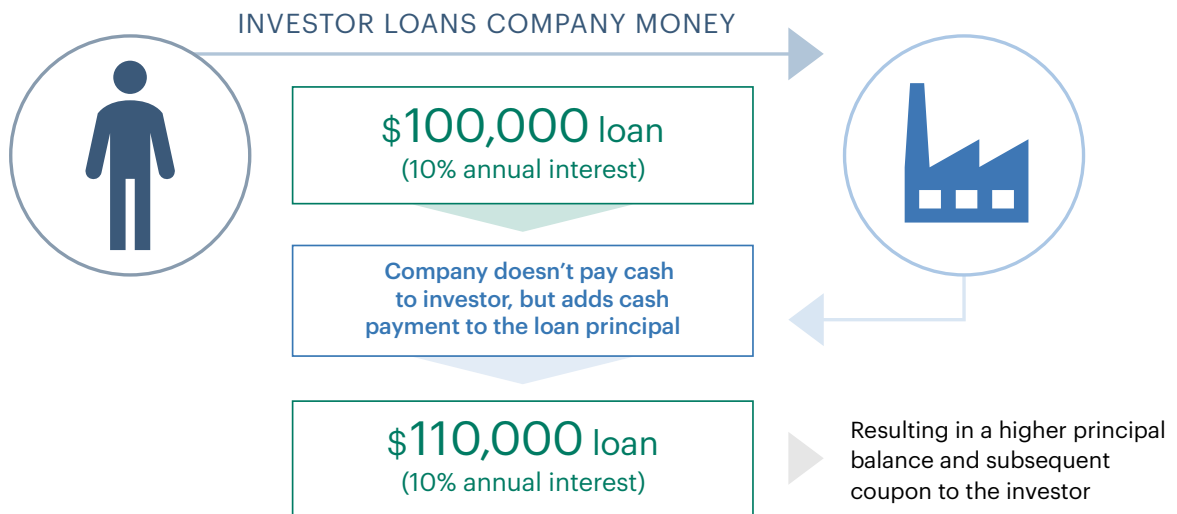
Exhibit 11: Larger companies are increasingly tapping private markets

US companies with revenue over \$100 million



Data as of November 2024. Figures may not sum to 100% due to rounding. Sources: S&P Capital IQ, Apollo Chief Economist

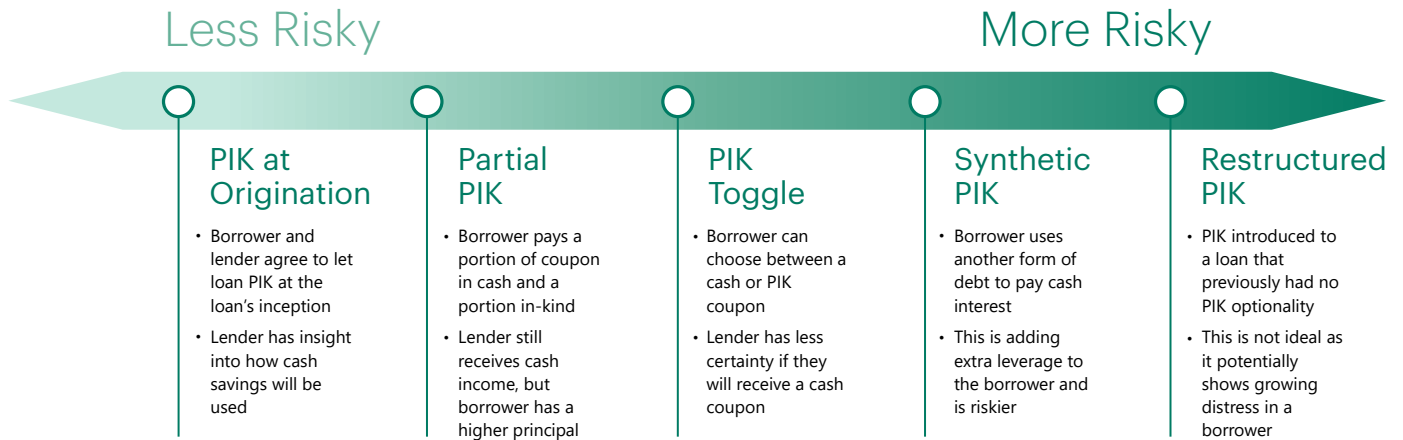
Exhibit 12: Quick primer on PIK and why it matters



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Exhibit 13: The lender’s perspective on PIK



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The Role of Private Credit in a Broader Asset Allocation

In today’s environment, where traditional fixed income allocations are reevaluated, private credit is emerging as an attractive alternative to the traditional “core-plus” strategy. Historically, that strategy has supplemented core bond exposure—like the Bloomberg Aggregate—with a 25% allocation to public high yield. But the data shows that

substituting private credit in place of public high yield can offer meaningfully better outcomes.

From January 2005 through September 2024, a core-plus portfolio that allocated 25% to private credit delivered an annualized return of 4.8%, compared to 4.1% for a portfolio that used public high yield. Perhaps more notably, the private credit version delivered this outperformance with lower volatility—3.4% versus 4.5% (**Exhibit 14**).

Exhibit 14: A modern approach to core plus



	Bloomberg Agg	Public High Yield	Private Credit	TRADITIONAL APPROACH (75% Agg / 25% Public High Yield)	MODERN APPROACH (75% Agg / 25% Private Credit)
JANUARY 2005– SEPTEMBER 2024					
Annual Return	3.2%	6.4%	9.3%	4.1%	4.8%
Standard Deviation	4.3%	10.5%	6.4%	4.5%	3.4%

For illustrative purposes only. Sources: Preqin, Bloomberg. Data accessed March 2025. Quarterly data from January 2005 to September 2024. Investments include Bloomberg US Aggregate Total Return Value Unhedged USD for fixed income, Preqin Private Debt for Private Credit and Bloomberg US Corporate High Yield Total Return Index for Public High Yield.

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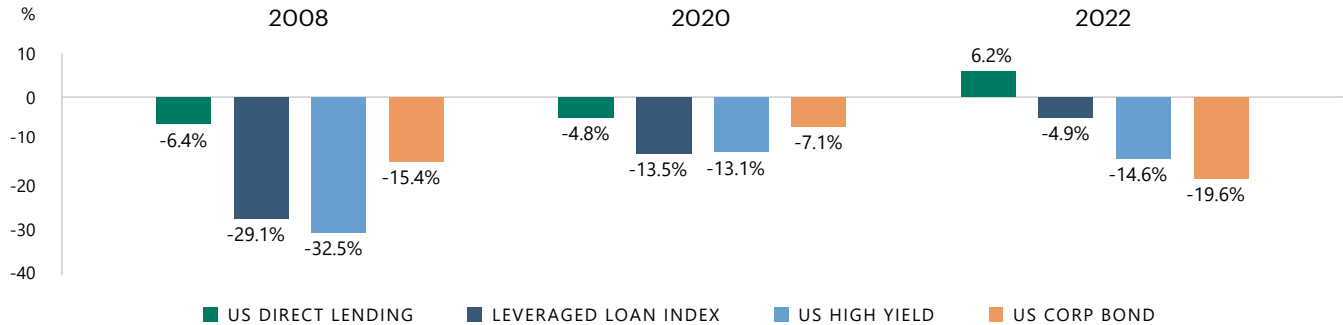
Unlike public high yield bonds, which are typically unsecured, subordinated, and fixed-rate, private credit loans are secured, senior in the capital structure, and floating-rate. These characteristics not only improve downside protection but also can enhance relative performance potential when rates rise or credit spreads widen. Due in part to these structural protections, private credit has historically weathered market downturns better than other parts of the credit spectrum.

During drawdowns in 2008, 2020, and 2022, the direct lending asset class outperformed high yield bonds, leveraged loans, and corporate bonds (**Exhibit 15**).

Taken together, we believe these advantages make a strong case for modernizing the core-plus allocation. In a world where traditional return sources are under pressure and volatility is rising, private credit can offer a way to enhance yield, reduce risk, and strengthen portfolio resiliency.

Exhibit 15: Direct lending demonstrated relative resilience during previous periods of market stress

Max drawdown during periods of market stress (%)



Sources: US Cliffwater Direct Lending Index, RHS Chart: Mornigstar Direct, Morningstar LSTA US LL Index TR USD, ICE BofA US High Yield TR USD, Bloomberg US Corp Bond TR USD as of December 31, 2024.

Conclusion: Navigating the Crossroads of Credit and Policy

Credit markets are entering a new phase—one shaped by macro uncertainty, shifting policy dynamics, and evolving borrower needs. The expansion of tariffs is not merely a headline risk; it is actively reshaping corporate behavior, suppressing consumer sentiment, and introducing strain into the foundational levers of economic growth. While larger borrowers remain relatively well-positioned, smaller issuers face mounting pressure from higher rates, rising costs, and weakening demand.

Against this backdrop, private credit remains both resilient and responsive—gaining ground not just as a source of new capital, but as a primary channel for refinancing and strategic funding. Its structural advantages over public high yield—senior secured positioning, floating rates, and bespoke terms—have helped it demonstrate strong performance during market stress.

Looking ahead, as private market financing continues to increase relative to public markets, demand for private credit is expected to grow with the increasing need for larger, more flexible financings.

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