



Who Gives a Hoot?

In late February, an alternative asset manager halted quarterly exits on one of its semi-liquid private credit funds. The gating of redemptions frightened investors at a time when AI fears were mounting and market valuations were wavering. Within days, broader credit markets began showing signs of fear.

For investors, it's crucial to understand the distinction between the structural issues around private credit fund structure, the true credit risks of the underlying assets, and the origins of systemic risk.

First, we should address what happened with these specific funds. A key point is the relationship between the non-traded assets and the publicly traded vehicle. The non-traded fund was supposed to raise capital privately, build a loan portfolio, then provide liquidity by merging into the publicly traded fund. In the meantime, investors were told they could redeem up to 5% of their shares for cash on a quarterly basis. The asset manager attempted to realize this merger in late 2025. However, since the publicly traded fund's shares traded lower than Net Asset Value, investors in the non-traded fund viewed this mechanism as a forced loss. Under pressure, the asset manager may have terminated the merger.

Simultaneously, the 'SAASpocalypse' was ripping through software stocks based on a narrative that AI will commoditize software. Relevantly, private credit is overexposed to software due to the large degree of private equity acquisitions in the sector.

The concurrent issues melded into a mega-narrative that private credit is a systemic risk on the verge of collapse. The shares of asset managers and publicly traded BDCs sold off sharply. Disaggregated, investors responded to three different narratives with differing implications and relevant timelines.

Liquidity

Are investors in private credit vehicles selling under the belief that the underlying assets are not performing? Do they have immediate needs? Or do they see other investors rushing toward the exits? Regardless of the motivation, if people are trying to redeem their shares in amounts greater than is permitted by the fund – generally 5% of shares per quarter – the gating of redemptions may be portrayed as a failure of the asset class. But, in our opinion, this criticism is misguided. The gates are key to functioning. The

underlying asset – the loans – do not trade on a sizable secondary market. A run on the funds would lead to fire sales of the loans and make it harder to distribute marginal redemption requests. The asset class is sold as illiquid; the illiquidity premium is supposedly the source of outsized returns. The vehicles should be re-branded from ‘semi-liquid’ to ‘hardly liquid.’ The fund structure tries to move these illiquid assets into a partially liquid vehicle. This structure works fine when stress is low, but most investors would want liquidity at the same time as everyone else.

Transparency

A big knock on private credit is the lack of continuous price action on the loans. External observers see funds move loan prices from par to zero instantly when borrowers default. For funds, there’s some logic to this. On their end, they see borrowers paying the interest until they stop paying. Alternatively, they can rework the debt with payment-in-kind – which converts cash payments into additional debt – or other mechanisms, so they can say that the borrower is technically paying in full. The fund structure is once again what connects the underlying loans to the pricing logic of the open market. The ZIRP era and private market boom allowed valuation practices to go largely unscrutinized. Investors don’t ask too many questions about valuation methods when returns are good, stress is low, and nobody’s demanding cash. When narratives turn, people start criticizing the valuation and pricing process. Investors start asking deeper questions about the nature of these assets. The angst turns ontological: what are prices and where do they come from? Are prices derived from a fundamental value or are they what a buyer is willing to give? In an efficiently traded market, these are supposed to be the same. In private credit, the assets are rarely traded. Value is a phenomenon of accounting on fund books, rather than expressed through exchange. In public markets, prices are meant to indicate the broad market opinion of credit quality. In private markets, value is an internal assessment. Produced not discovered. This distinction is irrelevant in calm periods but is critical when investors want to exchange their holdings and shares for real cash.

Credit Quality

The structural concerns about fund design and the larger macro narrative around software converge on the quality of the underlying loans. The structure and the narrative feed back into each other. Private credit is heavily exposed to software companies acquired by PE sponsors at high leverage multiples justified by recurring revenues and large profit margins. If AI commoditizes software and compresses margins, the ability to service debt deteriorates. When this concern – which has not been observed in earnings data – arises, the fund structure can add fuel to the fire. In public markets, opinions on credit risk can be expressed through transactions; the changing price is a public signal. In private markets, market participants are free to imagine the value of underlying assets. There is no published earnings data on the underlying borrowers. When times are good, actors can assume the loans are more valuable than they are so there’s no volatility. When crisis hits, actors can project larger losses than the loan would have if publicly traded. They seek the closest avenue to price discovery through transaction: the redemption of fund shares. When the asset managers

gate redemptions, investors ask: are they keeping me in the fund because the assets are not as valuable as the manager says? The three concerns are mutually reinforcing. Together they create a feedback loop that looks like systemic risk even if the actual credit losses turn out to be modest. However, the credit could be that bad. We cannot know until a borrower defaults; there's no published data on debt coverage capacity. But the point remains: the structural issues around fund design are not themselves evidence of deteriorating credit quality. They are evidence that the vehicle is not built for stress.

The drama spread to the rest of the private credit industry. The fund structure problems collided with a macro narrative and created suspicion about the whole sector. The '2008 again' comparisons are everywhere online; any collateralized structure or bit of leverage is seen as a reincarnation of subprime mortgage lending and CDOs. The question of systemic risk and interconnection is real. Private credit sits between private equity leverage, bank lending, insurance company balance sheets, and institutional allocation to alternatives. However, this incident is not a systemic meltdown but a stress test of semi-liquid vehicle design. When a true credit crisis happens – exposing variation in underwriting standards – and private credit losses propagate through the financial system, transmission channels will matter more than narrative.

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