ALTERNATIVE CREDIT COUNCIL
LENDING FOR GROWTH

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THE ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION
ALTERNATIVE CREDIT COUNCIL
PRIVATE CREDIT

ACC: Private Credit Q2 2026 Quarterly Update

Executive summary

- **Q2 data shows more stability than stress:** Loan valuations remain broadly healthy but the bifurcation between performing and stressed loans has deepened since Q1 2026. 85% of loans were valued above 97% of par, while the percentage of loans valued below 90% of par edged up from 5% to 7%. This cohort remains concentrated in identifiable sectors – particularly software – and in smaller borrowers, where 12% of loans in the $10–20mn EBITDA (earnings before interest, tax, depreciation and amortisation) bracket are priced below 90% of par.
- **Borrower earnings continue to improve:** Median revenues rose 6.5% and EBITDA rose 7.4% year-on-year in Q2 2026, extending the current period of margin expansion by another quarter. In plain terms, the typical borrower is generating more operating profit per dollar of revenue than it was three years ago - a sign of sustained operating discipline.
- **Most borrowers remain well placed to meet their interest payments:** Interest coverage ratios -a key measure of debt serviceability - remain near their recent highs at a median of 1.72x. The share of borrowers with coverage below 1.00x ticked up to 14.1% – the first increase in six quarters, but still well below the peak of 23.2% observed in December 2023. The dollar value of amended PIK loan interest (often stress driven) remains very low at 1.6% of total interest dollars.
- **This quarter's focus examines Business Development Companies (BDCs), using data from Raymond James and Cliffwater:** This shows that after falling sharply in Q1, public BDC prices rebounded decisively through Q2 and into early Q3. The Cliffwater BDC Index has returned +7.4% in Q3 to date, and the sectors discount to NAV narrowed from 24% in March to 10% by mid-August.
- **This data also provides evidence that the initial market reaction ran well ahead of credit fundamentals at the time:** NAV-based returns on the underlying loans remained positive throughout. Q2 filings show NAV declines moderating, non-accruals near 1% for large private BDCs, and unsecured debt markets firmly open, with approximately $7.5bn of index-eligible issuance in Q2 alone.

Core market indicators

Valuations: Normalising marks, with bifurcation by borrower size continuing

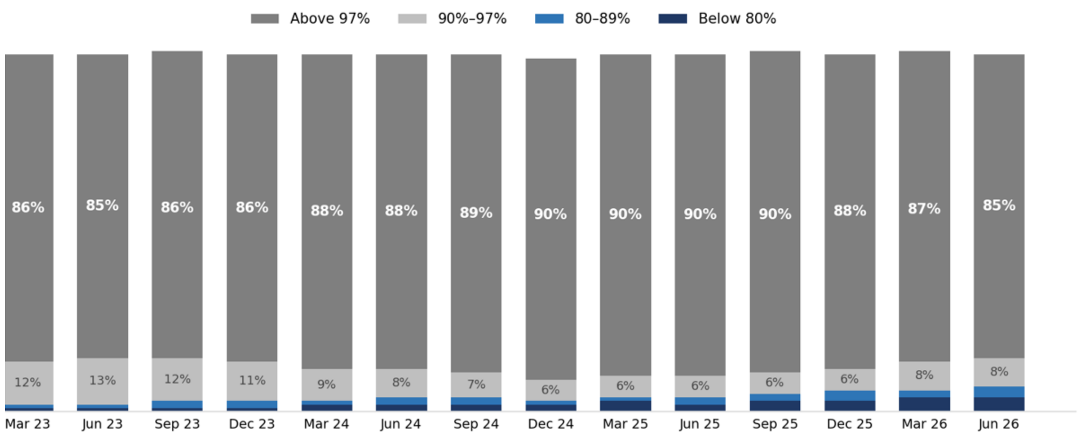
Loan valuations remain healthy in aggregate although the gap between the strongest and weakest borrowers has widened in the past quarter. As of Q2 2026, 85% of loans tracked by Houlihan Lokey were valued above 97% of par (i.e. very close to the amount originally lent), while the share of loans valued below 90% of par edged up from 5% to 7% over the quarter. The most deeply discounted tier – loans valued below 80% of par – account for 4% of loan portfolios.

Quarter-on-quarter valuations nonetheless normalised after the Q1 dislocation: 76% of loans were marked up in Q2, and meaningful markdowns fell back to 14% from 34% in Q1 – both within historical ranges observed over the prior eleven quarters.

Size remains a clear differentiator: 12% of loans to borrowers in the $10–20mn EBITDA bracket are valued below 90% of par compared to 6% for borrowers with EBITDA between $20-100 million. Borrowers above $100mn EBITDA continue to show the smallest share of discounted debt. This is intuitive – larger companies typically have more diversified revenues, larger balance sheets, deeper management teams, and greater ability to absorb shocks.

Historical Pricing Loan Prices by Bucket: All Borrowers

Fair Value Trend of All borrowers



Note: Figures may not total 100% due to rounding.

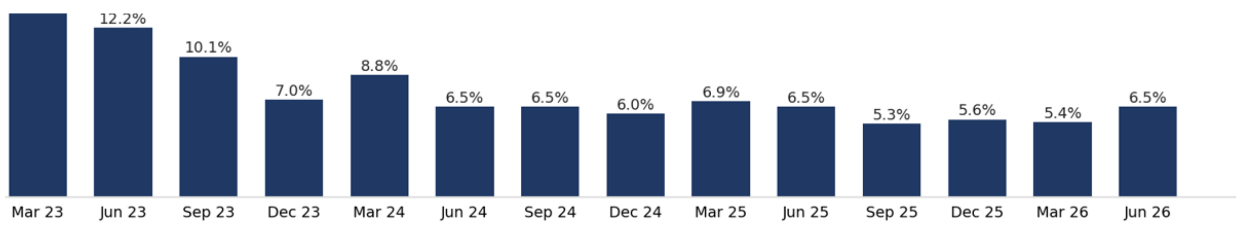
Source: Houlihan Lokey DataBank.

Earnings: Margins improving for a 11th consecutive quarter

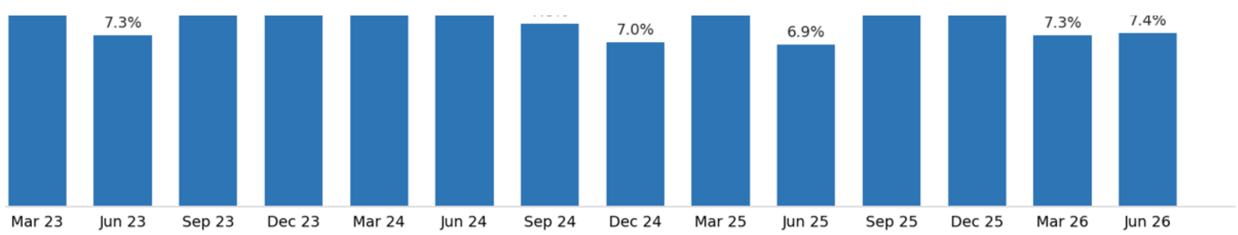
Borrower earnings continue to improve: Median revenues grew by 6.5% year-on-year, while EBITDA increased by 7.4%. Top-line growth accelerated from the prior quarter, and EBITDA growth has now outpaced revenue growth since Sep 2023, implying continuous margin expansion in that period. In plain terms, the typical borrower within the portfolio is generating more operating profit per dollar of revenue than it was three years ago – a sign of sustained operating discipline.

By sector, financial institutions recorded the strongest year-on-year (YoY) revenue growth at 16.0%, while technology, media and telecoms recorded the slowest growth at 4.1%. On profitability, healthcare led with 16.1% median EBITDA growth, with technology, media and telecoms again at the bottom at 1.4%. Notably, the independently tracked software cohort posted resilient growth despite prevailing market narratives around AI disruption to the sector.

Median Revenue Growth



Median EBITDA Growth



Credit metrics: Leverage stable, interest coverage plateaus at healthy levels

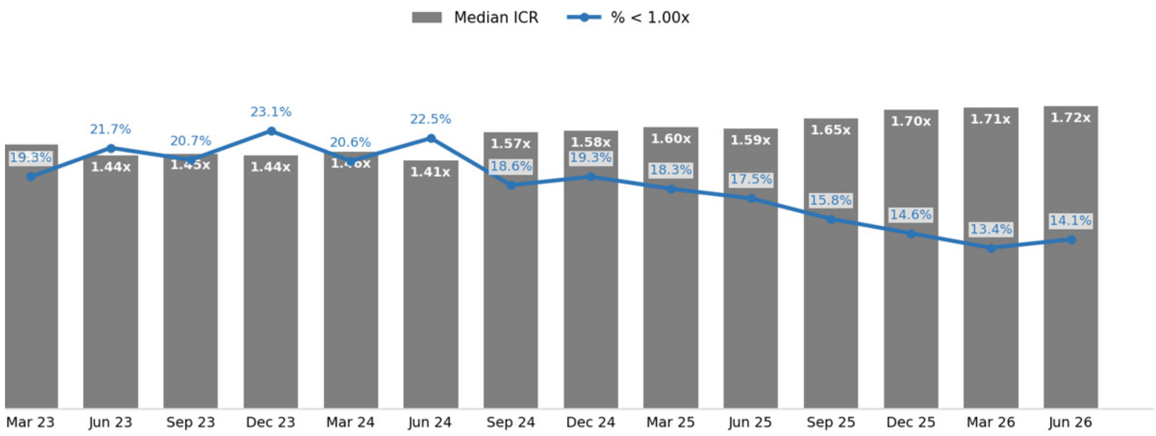
Leverage – the ratio of debt to EBITDA – remains broadly stable, with median net leverage of 4.56x across all borrowers. The familiar size hierarchy persists: larger borrowers sustain higher leverage because lenders view their diversified operations as lower risk, though the gap between the largest and smallest cohorts narrowed marginally in Q2.

Interest coverage ratios (ICR) – the multiple by which EBITDA covers interest expense and a key measure of debt serviceability – reached 1.72x in Q2 2026. This is the highest level in this data series albeit the pace of improvement has slowed, with the median advancing just 0.01x compared to gains of 0.03x in each of the two prior quarters. Median EBITDA growth of 7.4% would ordinarily lift interest coverage more meaningfully. However, yields rose across all borrower cohorts in the first half of 2026 as markets scaled back expectations of near-term rate cuts, and higher financing costs absorbed most of the operating gain.

The share of borrowers with ICR below 1.00x rose to 14.1% from 13.4% – the first increase in six quarters – but remains far below the 23.2% peak recorded in December 2023. Over 90% of private credit loans are floating-rate, meaning that borrowers' debt obligations are materially impacted – both positively and negatively – by interest rate moves.

Interest Coverage

Borrower Interest Coverage ratios



Note: ICR is calculated as EBITDA / total interest expense. Source: Houlihan Lokey DataBank.

Quarterly focus: Business Development Companies (BDCs)

Public BDCs offer a useful window into private credit portfolios. Over the past two quarters they have told a story in two acts: a sharp, sentiment-driven de-rating in the first quarter as AI and software headlines dominated, followed by a decisive rebound through the second quarter and into the third.

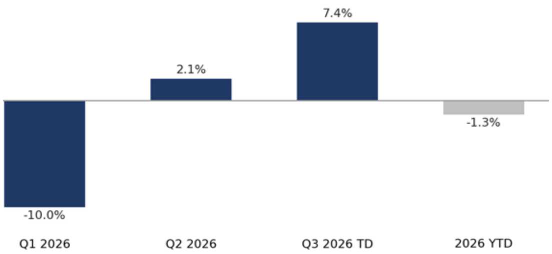
This section examines that rebound – and what the gap between market pricing and NAV-based returns says about how far the initial market reaction overshot. The analysis draws on Raymond James' Q2 2026 BDC Market Update (market data as of 20 August 2026, portfolio data from Q2 SEC filings), the Cliffwater BDC Index (CWBDC) and Cliffwater Direct Lending Index (CDLI).

The rebound: BDC equities recover as the discount to NAV narrows sharply

The Cliffwater BDC Index fell roughly 10% in the first quarter as investors priced in AI-disruption and potential credit risk. That move has now largely reversed: the index returned +2.1% in Q2 and a further +7.4% in the third quarter to date (through 14 August), as public equity markets rallied and investor sentiment improved on the back of Q2 results. The clearest illustration of the swing in sentiment is the sector's discount to NAV, which widened to 24.1% at the end of March – a level seen only briefly during the 2020 and 2022 sell-offs – before narrowing dramatically to 10.3% by mid-August, back within its longer-run trading range.

The speed and scale of the recovery is instructive. Share prices swung by more than 15 percentage points from peak-to-trough and back, yet the NAV-based returns on the underlying loans barely moved. The CDLI – an unlevered, fee-free index of directly originated middle-market loans – returned +1.89% in Q2 and +7.71% over the trailing year. This has been driven by interest income of 9.9% with realised losses of just 0.47% over the same four quarters. The public loan market corroborates the turn: after falling 7.68% in Q1, syndicated software loan prices stabilised in Q2 and have returned +1.93% in the third quarter to date. Taken together, the round-trip in public pricing against essentially stable credit fundamentals suggests that Q1 negative sentiment ran well ahead of the underlying data.

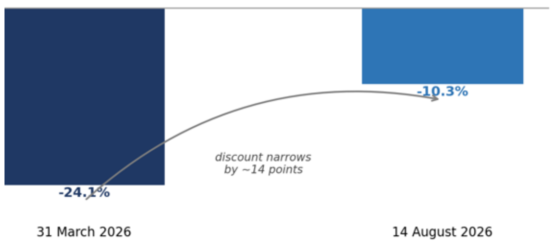
Cliffwater BDC index total return



Q3 2026 TD and YTD through 14 Aug 2026.

Source: Cliffwater.

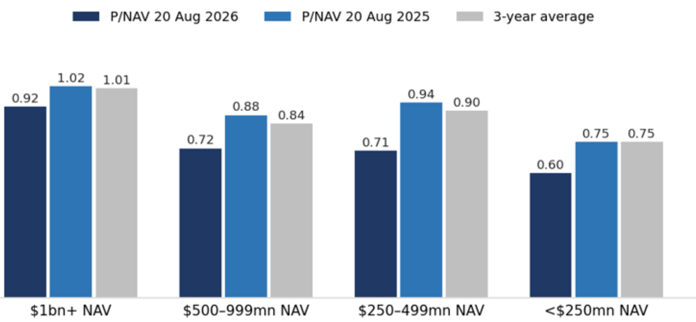
CWBDC Premium / Discount to NAV



Source: Cliffwater. BDC index

Despite the recent recovery, BDCs continue to trade at a discount to NAV with a clear divide between larger and smaller firms. BDCs with over $1bn of NAV trade at an average of 0.92x NAV, compared with 0.60x for those below $250mn, mirroring the size-based credit dispersion in the loan-level data above. Market pricing of this kind is itself a form of discipline unique to the listed part of the asset class. Discounts constrain equity issuance (BDCs generally cannot issue below NAV without shareholder approval), so capital formation self-corrects with sentiment – and re-opens as it recovers. The sector's average dividend yield of 13.68% still offers roughly nine percentage points over 5- and 10-year US Treasuries.

Price / NAV by BDC size



Public BDCs, grouped by NAV, as of 20 Aug 2026.

Source: FactSet, Raymond James.

Portfolio fundamentals: NAV pressure moderating, credit stress contained

BDC NAVs saw similar normalisation in Q2 to that observed in loan valuation data. Pressure eased materially in the second quarter with average quarter-on-quarter NAV declines for public BDCs easing from -3.3% in Q1 to -1.0% in Q2. The same trend was observed in larger private BDCs, where the decline narrowed from -1.4% to -0.4%.

Non-accruals – loans on which a BDC has stopped recognising income – averaged 4.2% of cost for public BDCs in Q2 (up modestly from 4.1%) and just 1.1% for large private BDCs (down from 1.2%).

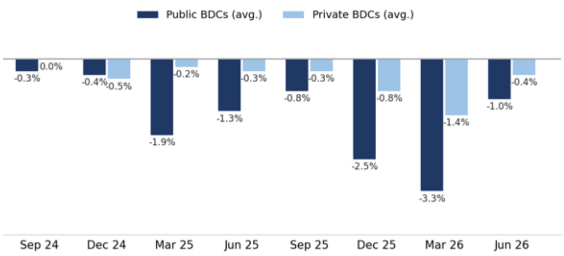
There are two important points to consider when looking at these figures. First, dispersion is wide with sector averages negatively affected by a small number of vehicles with legacy or venture-lending portfolios. Second, private BDCs – which hold the bulk of the newer, predominantly first-lien vintage of direct lending – show non-accrual levels around 1%, consistent with the low cumulative loss ratios for first-lien direct lending discussed in last quarter's update.

Payment in Kind (PIK) income averaged in the high single digits as a share of total investment income for public BDCs, with substantially lower levels across most large private BDCs – again consistent with the loan-level finding that stress-driven PIK remains a small fraction of interest dollars. Portfolios remain heavily first-lien oriented, and BDCs' own interest coverage of their funding costs typically runs at 2–3x.

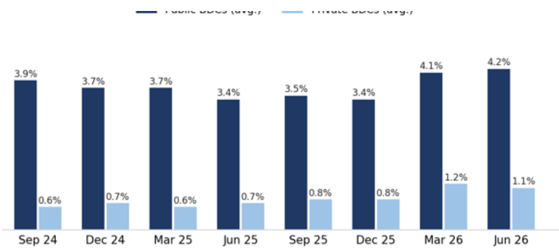
The CDLI provides useful context on where the residual pressure sits within portfolios and the likelihood of this crystallising. Trailing four-quarter net unrealised losses stood at 1.59% of assets as of June and are highly concentrated. 62% of these unrealised losses come from software but this sector represents only 24% of index assets at cost. These software loans have been marked down by 4.1% which equates to around 1% of the value of all loans in the index. Software is therefore responsible for most of the deterioration in valuations, but the impact of this on portfolios remains relatively small.

Two decades of CDLI history also show that unrealised marks systematically overstate eventual losses. Historically only around half of unrealised losses have converted into realised losses. The current 1.59% is also much lower than unrealised troughs of 16.3% in 2008 and 7.4% observed in 2020. Realised losses over the trailing year were 0.47%.

Quarter-over-quarter NAV change



Non accruals as % of cost



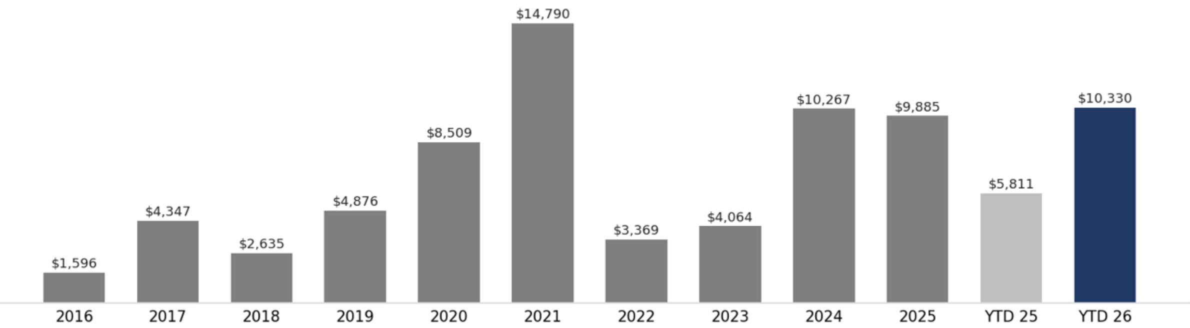
Averages. Private BDCs = $750mn+ AUM.
Source: SEC filings.

Funding markets: Firmly open, with growing unsecured issuance

Debt capital markets issuance – a key indicator of investor confidence in the sector – accelerated through the first half of 2026. Public BDCs have issued $10.3bn of capital year-to-date compared to $5.8bn raised over the same period in 2025, driven primarily by unsecured debt offerings as private and perpetual BDCs issued approximately a further $6.8bn of debt. In Q2 alone there were 14 'index-eligible' unsecured bond issuances ($300mn or larger) totalling roughly $7.5bn, with new issuance from managers across the size spectrum pricing at spreads of roughly 180–330bps over Treasuries.

The shift toward unsecured, term funding with staggered maturities is structurally positive. It reduces reliance on secured bank facilities, unencumbers assets, and spreads refinancing needs over time. Public equity issuance, by contrast, remains limited while many BDCs trade below NAV, the self-correcting discipline noted above.

Public BDC Financing Activity ($mn)



Public BDC financing activity only; excludes private/perpetual BDC debt issuance. YTD as of 20 Aug 2026.

Source: FactSet, SEC filings.

Distributions: Resets aligning payouts with earnings

Dividend resets broadened through 2026, with base distribution reductions at a number of public BDCs in Q2. These were typically in the range of 7–25%, with a small number of larger cuts following significant reduction activity in Q1. These resets are principally a function of lower base rates feeding through floating-rate portfolios and tighter asset spreads rather than realised credit losses. These resets represent distribution discipline working as intended with payouts aligning with recurring earnings rather than being sustained at the expense of NAV erosion. Larger perpetual BDCs also saw modest equity contraction over the first half of 2026 (for example, the largest fund's net assets declined from $47.6bn to $42.8bn), with repurchase requests managed in an orderly fashion within their stated quarterly limits. This offers further evidence that the semi-liquid structure absorbs redemption pressure without requiring forced asset sales. Wealth and institutional investor channels have, notably, diverged in sentiment. Wealth-channel perpetual BDC flows turned negative in the first half, whereas institutional private debt fundraising is on track for a record year in 2026. This is a useful reminder that the investors closest to the underlying credit data have continued to allocate capital through the volatility.

Conclusions

- **Q2 marked a normalisation, not an all-clear.** Markdown activity stabilised in Q2 although some areas of market weakness remain. After the Q1 dislocation, markups returned to their historical range while declines in BDC NAV slowed significantly. However, the most severely marked down cohort of loans remains around double its historical level, and loans valued below 90% of par are up slightly from the previous quarter. Stress is contained, but it has not disappeared.

- **Stress remains concentrated among smaller borrowers and in the software sector.** 12% of loans to borrowers in the EBITDA range $10-20mn are valued below 90% of par, roughly double the broader market average. Software markdowns also broadened in the first half of the year. This segment may warrant focus from supervisors interested in SME credit conditions as it largely sits outside the traditional bank lending channel.

- **Positive fundamentals across key indicators.** Borrower earnings have delivered a 12th consecutive quarter of margin expansion, interest coverage sits at series highs, and amended PIK remains 1.6% of interest dollars. The sub-1.00x coverage uptick and rising yields are the forward-looking watch-points.

- **BDC rebound suggests that Q1 sentiment overshot fundamentals.** Public BDC equities have recovered most of their first-quarter losses, with the sector's average discount to NAV narrowing from 24% in March to 10% by mid-August. NAV-based loan returns were positive throughout and realised losses ran below half a percent over the trailing year. Other indicators also remain broadly positive. Filings show that NAV declines have slowed, non-accruals among large private BDCs remain around 1%, BDCs continue to have access to debt markets and institutional fund raising remains strong. Taken together, this data suggests that the sharp fall in public BDC valuations in Q1 was greater than the deterioration seen in their underlying loan portfolios.

Data sources

Unless otherwise cited The ACC Quarterly Update incorporates data from the Houlihan Lokey DataBank which covers 70,000+ loan valuations and contains hundreds of loan-level metrics and standardized fields stemming from Houlihan Lokey's recurring portfolio valuation work dating back to 2017. Data is accumulated at monthly, quarterly, or annual intervals over most of an investment's holding period to provide a comprehensive time-series view of portfolio company performance, credit quality, market benchmarking, and valuation outcomes throughout a loan's lifecycle.

The Quarterly Focus section incorporates data from the Raymond James Investment Banking Q2 2026 BDC Market Update, based on SEC filings, company disclosures, FactSet and Bloomberg, with market data as of 20 August 2026 (private BDC figures represent private BDCs with over $750 million in AUM), and from Cliffwater's Q2 2026 update on the Cliffwater Direct Lending Index (CDLI) and Cliffwater BDC

ACC is the private credit affiliate of AIMA, the world's largest membership association for alternative investment managers