Cresset Partners

Introduction to Direct Lending

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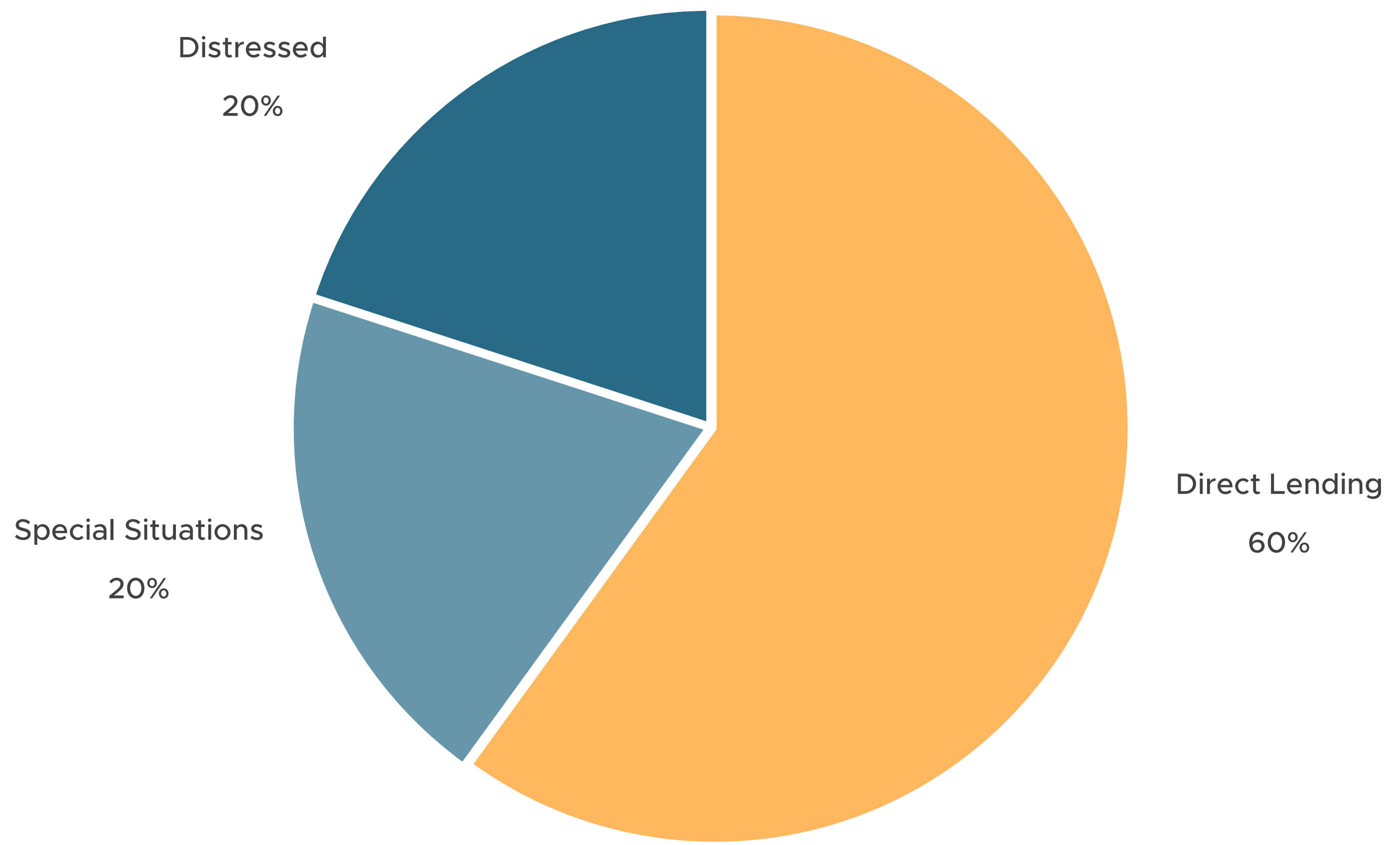
Private Credit Market Today

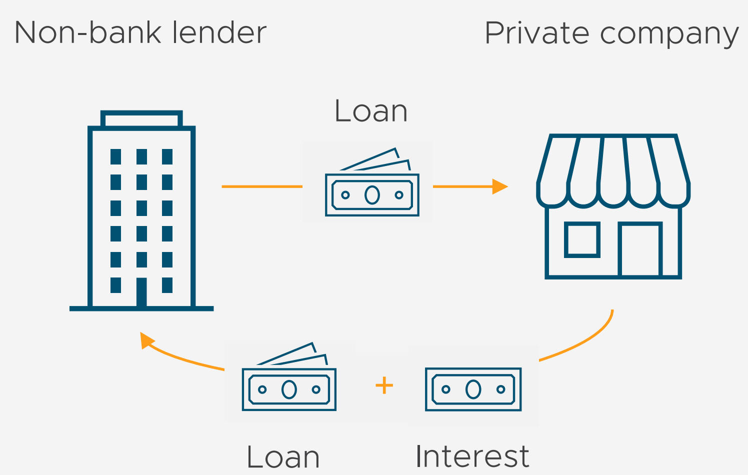
Direct Lending is the predominant asset class in the Private Credit market.



Source: North American Private Credit Market Overview data from Preqin as of 12/31/21

Direct Lending

Direct Lending includes any debt held by—or extended to—privately held companies.
The strategy most commonly involves non-bank institutions making loans to private companies.



The private company must pay back the full sum of the loan, plus interest, to the lending institution.

Direct Lending: Investment Thesis

Why Direct Lending?

- All-weather strategy
- Consistent current income
- Historically low default rates[1]
- Floating rate loans provide a natural hedge against rising interest rates
- Premium yields above public fixed income[2]

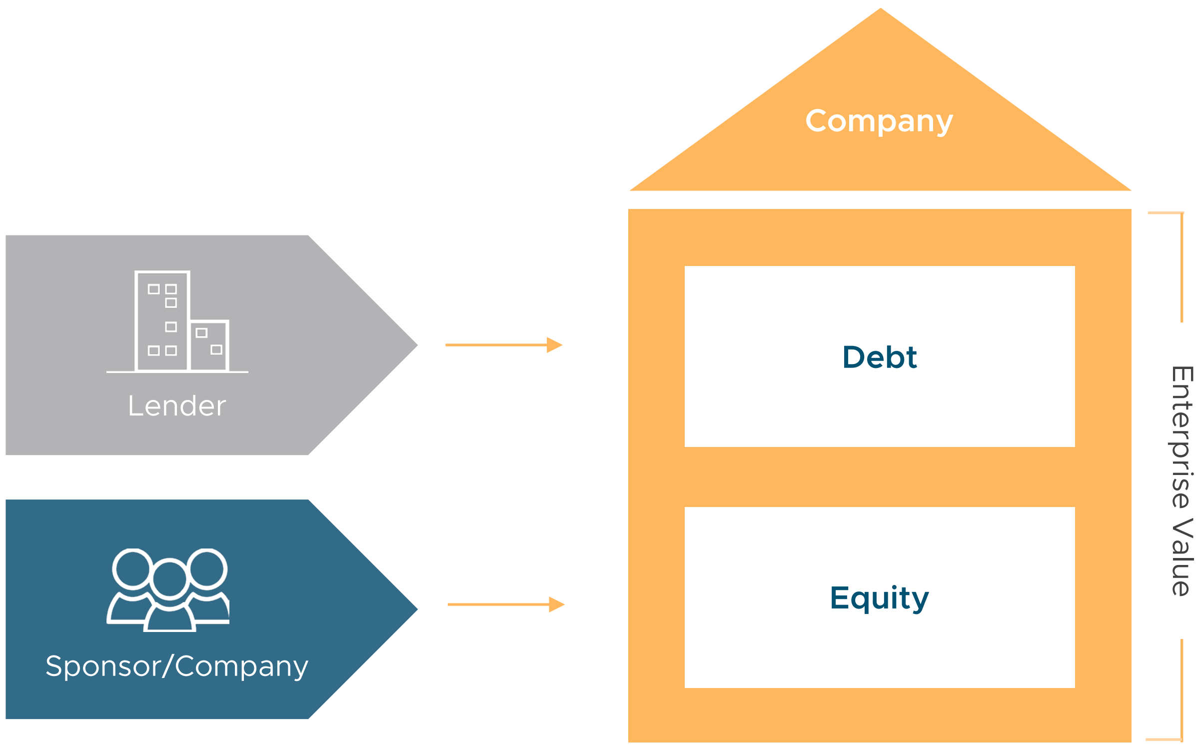
Why Now?

- Greater private equity dry powder increases demand for Direct Lending
- Traditional bank financing has declined, providing an opportunity for private non-bank lenders
- Recent market volatility has led to spread-widening, providing a compelling environment to deploy capital into Direct Lending

1. Credit Pro/Loss Stats, S&P Global Market Intelligence. 2. Preqin Insights 2022 Alternatives in North America report

Sponsor-Backed Lending

Lending to companies owned or controlled by a Private Equity Sponsor:



- Sponsors and lenders have an aligned interest: the success of the Company.
- Having another source of capital (Sponsor equity) mitigates the risk to the lender that the Company would need to take on additional debt.

The Capital Stack

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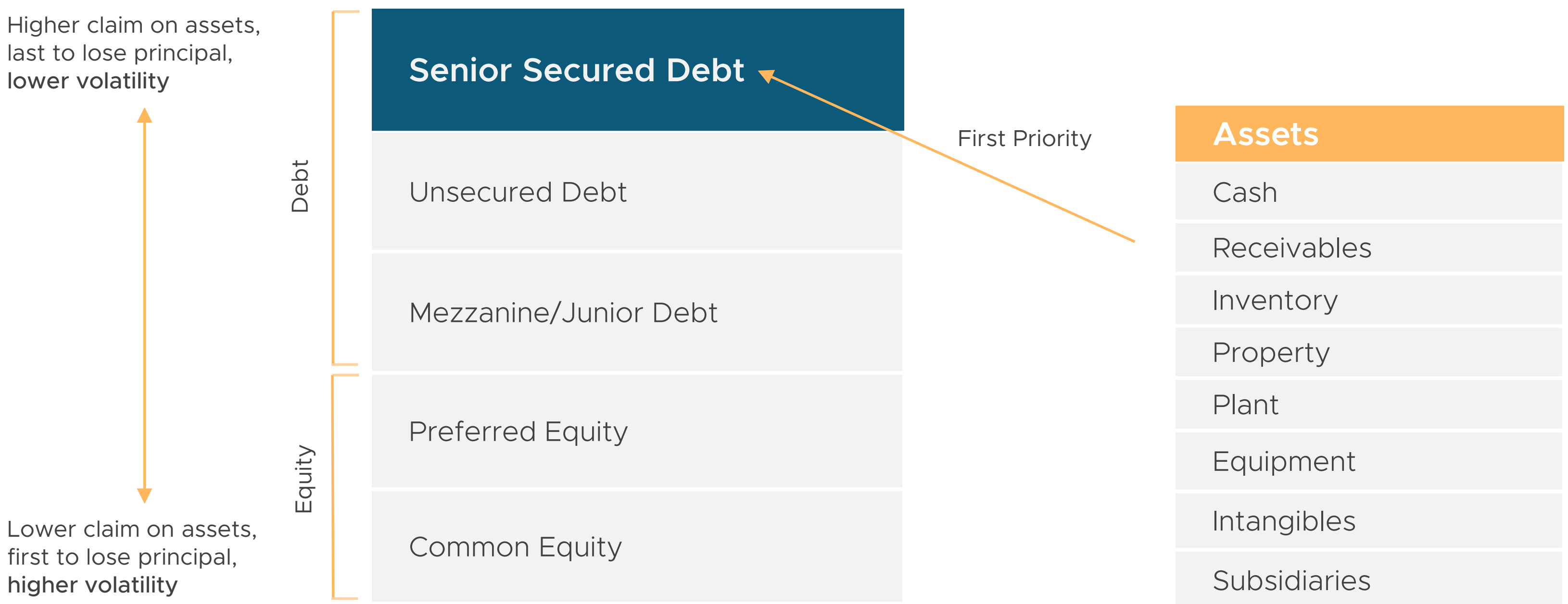
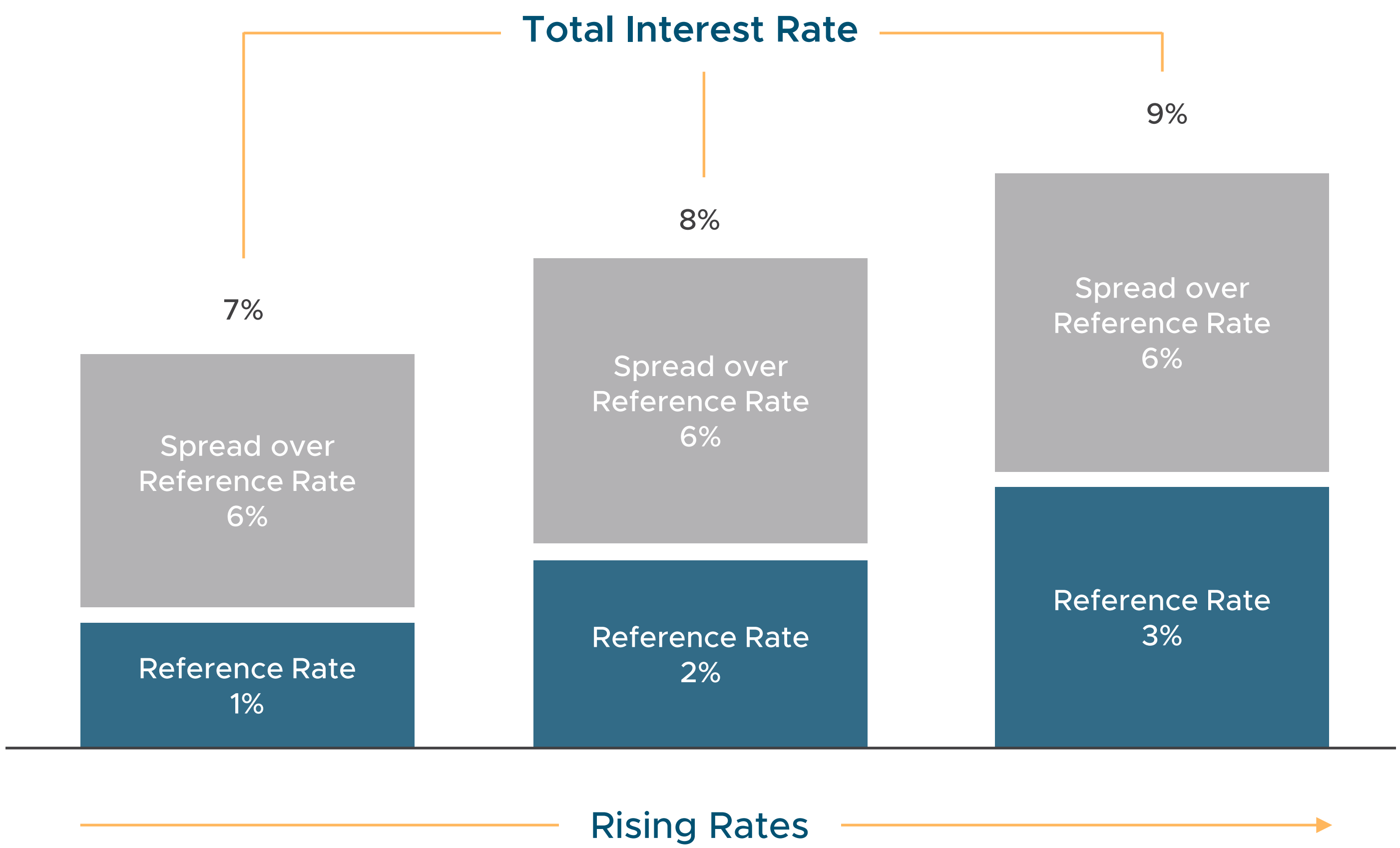
Direct loans are typically senior in the capital stack, secured by collateral and offer floating interest rates.



- A company's capital stack dictates repayment prioritization for the competing interests of owners and creditors, especially with respect to claims on its cash flows and assets. Senior secured debt is widely viewed as the safest part of the capital stack as these claims are first to be repaid in the event of a default.
- Senior secured loans typically have recourse to the cash flows, assets, and enterprise value of the borrower.

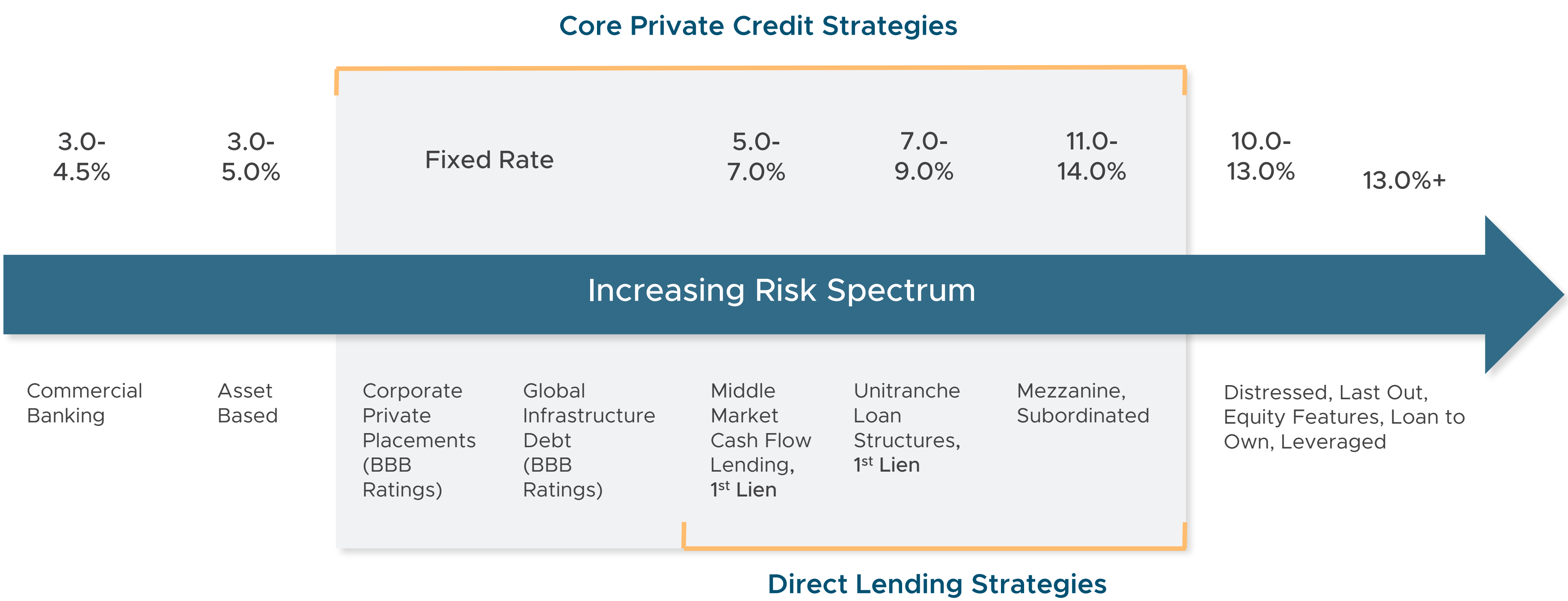
Floating Interest Rates

As SOFR increases, the borrower's overall interest rate increases.



Interest Rate Spreads

Interest Rate Spreads are priced on a risk spectrum.



For Illustrative Purposes Only. Return ranges are gross and are based on Barings' market observations as of December 31, 2021.
There is no guarantee illustrated ranges will be achieved.

Covenants

Covenants require the borrower to maintain certain financial standards and metrics.

Covenant Examples	
Maintenance/ Financial Covenants	Examples include: • Interest coverage • Maximum leverage • Fixed charge coverage
Incurrence Covenants	Examples include: • Restrictions on debt issuance • Dividend repayment • Fixed charge coverage • Share purchase • M&A or divestiture

- In the event of a covenant default, the lender has authority to renegotiate the terms of the loan agreement.
- Covenants have historically driven higher recovery rates and lower default rates in the direct lending market than in the public debt markets[1].

1. S&P Global LossStats

In Summary

+ Direct Lending is an "All-Weather" strategy with an attractive risk/return profile.
+ Sponsor-backed lending provides additional borrower support and downside mitigation.
+ Senior Security and Covenants drive higher recovery rates and lower default rates than in the public debt markets.
+ Floating Interest Rates provide a natural rising-rate hedge.
+ See pages 12 and 13 for a Glossary with defined terms used throughout this presentation.

Glossary

Glossary

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Terms	Definitions
Capital Stack	Order of repayment for a company's obligations, including debt and equity.
Co-Investments	Investing alongside a private credit manager. As opposed to being a participant in a fund, a co-investor directly owns a portion of a loan that is allocated to and ultimately controlled by the private credit manager.
Collateral	Assets pledge for repayment of a loan.
Default or Event of Default	An occurrence in which a borrower fails to comply with the loan agreement.
Direct Lending	Loan between a non-bank financial institution and a corporate borrower.
Distressed Debt	Debt associated with a company that is in or likely to enter bankruptcy.
Dry Powder	Cash that has been committed by investors but has yet to be called or deployed by an investment manager (cash available for an investment).
EBITDA	Earnings before Interest, Taxes, Depreciation and Amortization
First-Priority or First Lien	The first obligation in the capital stack waterfall. In an event of default or liquidation, this is the first debt obligation fully paid.
Fixed Income Investing	Investing focused on preservation of capital and current income under which the borrower or issuer is obliged to make payments of a fixed amount on a fixed schedule.
Floating Rate	Floating rate loans are priced as a spread (%) above a reference rate, such as SOFR. Floating-rate interest rates are subject to changes as a result of daily movements in SOFR. Borrowers with floating rate loans are responsible for paying the lender: SOFR + Spread = Interest Rate paid by the borrower.
Illiquidity Premium	Any form of additional compensation that is required to encourage investment into assets that cannot be easily and efficiently converted into cash at a fair market value.
Junior/Subordinated	Debt issued with a lower priority for repayment than senior debt.
Leverage	Borrowed capital.
Leverage Ratio	The level of debt held by a business divided by other measures of the company's balance sheet or income statement. Generally, in direct lending, leverage refers to Debt/EBITDA to measure the company's ability to repay debt.

Glossary

Terms	Definitions
Leveraged Buyout	The acquisition of a company using debt as a source of financing.
LIBOR	London Interbank Offered Rate – A benchmark interest rate that indicates borrowing costs between banks. Prior to 12/31/21, Direct Lending interest rate spreads were typically quoted as a spread above LIBOR. Since 12/31/21, new loans have not been permitted to use LIBOR as a reference rate as LIBOR has been replaced by SOFR.
Loan Close or Loan Closing Date	The effective date of a loan agreement.
Mezzanine Debt	Debt issued has conversion rights to equity with embedded equity options if the borrower defaults.
Middle Market Company	Typically defined by companies generating EBITDA of $10-100 million annually.
Non-Bank Lender	Lenders source and structure each transaction and negotiate the terms of the deal directly with the borrower or Sponsor.
Reference Rate	An interest rate benchmark. The most common reference rate used in direct lending is SOFR.
Rising Rate Environment	When interest rates and borrowing costs increase, typically driven by the Fed or market conditions, which in turn increases reference rates. The dynamics of SOFR are closely linked to the dynamics of the Fed Funds rate, which helps floating rate loans hedge inflation-risk.
Second Lien	The second obligation in the capital stack waterfall. In an event of default, this is the second debt obligation fully paid.
Secured	The asset that is provided as collateral to help lower financing costs. In an event of default, the lender can claim the borrower’s cash flows, assets, equity, IP, etc.
Senior	First tier in the capital stack waterfall. Senior can be further classified as First Lien or Second Lien.
SOFR	Secured Overnight Financing Rate – A nearly risk-free reference rate that measures the cost of borrowing cash overnight collateralized by U.S. Treasury Securities. This reference rate replaced LIBOR.
Special Situations	A loan based on a ‘special situation,’ referring to something other than the underlying company fundamentals.
Sponsor	When a company is owned by a private equity fund, the fund’s General Partner (GP) is often referred to as the sponsor. The fund is the investment capital used to buy a controlling interest in a company, and the sponsor is responsible for operating the fund.
Underwriting	The process through which an institution evaluates financial risk.

Q&A