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The Convergence of Public and Private Markets: The Rise of Private Credit

The growing integration of public market participants into private markets marks a paradigm shift in the investment world. Private credit stands out as a compelling opportunity, offering strong yield potential, portfolio diversification, and resilience against public market volatility.

In recent years, the investment landscape has undergone a fundamental shift. Traditional public market participants, including asset managers and institutional investors, are increasingly allocating capital to private markets. This convergence is driven by a confluence of factors, including the pursuit of higher returns, diversification benefits, and the opportunity to invest in assets less correlated with the volatility of public markets. Among the various private market asset classes, private credit has emerged as a particularly attractive avenue, bridging the gap between traditional fixed-income investments and private equity-style returns.

The Drivers Behind the Shift

Historically, institutional investors such as pension funds, endowments, and sovereign wealth funds have primarily focused on public equities and fixed-income securities. However, the past two decades have seen diminishing returns from traditional asset classes due to persistently low interest rates, heightened market volatility, and increasing competition in public markets. These challenges have prompted investors to explore alternative sources of yield and stability.

Several key factors have accelerated this trend:

- **Enhanced Return Potential**
  Private markets, including private credit, can offer superior returns compared to traditional bonds and publicly-traded equities. Unlike public markets, which are characterized by high liquidity and efficiency, private markets present opportunities for investors to seek long term, stable returns, rather than be at the whim of daily volatility and market risk.

- **Diversification Benefits**
  Private assets exhibit different behaviors and less volatility than public market fluctuations, making them valuable for portfolio diversification. By allocating capital to private credit, investors can reduce their exposure to systemic market risks while benefiting from steady income streams.

- **Structural Market Changes**
  The regulatory tightening on traditional banks since the 2008 financial crisis has restricted their ability to extend credit to mid-market businesses. This has created a vaccum in lending that private credit lenders are able to fill with products offering investors higher returns.

- **Technological Advancements and Market Access**
  The democratization of financial data, improved reporting standards, and the rise of investment platforms specializing in private credit have made it easier for public market investors to access private opportunities. These innovations have lowered traditional barriers to entry, enabling asset managers to deploy capital more efficiently.

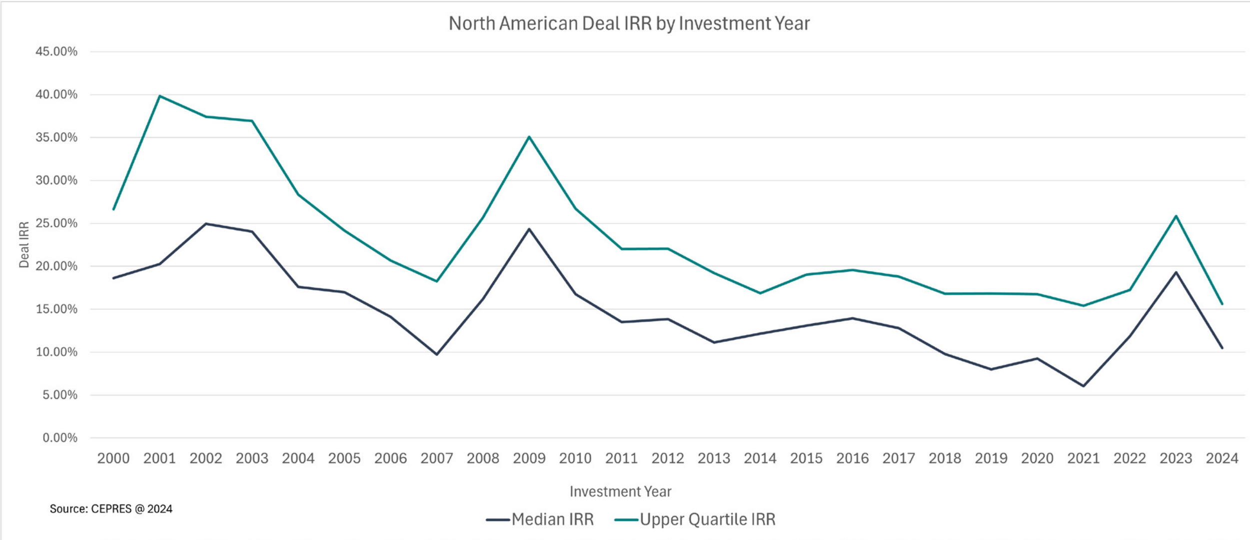
Private Credit as a Key Facilitator
Among the various private market asset classes—such as private equity, real estate, and infrastructure—private credit, in the form of direct loans, mezzanine financing, distressed debt, and special situations investing has gained significant traction as an alternative to traditional debt instruments for the following reasons:

- **Predictable Cash Flows**
  Unlike private equity, where returns are often backloaded, private credit provides more immediate and predictable cash flows through interest payments. This characteristic makes it particularly appealing to institutional investors seeking yield in a low-interest-rate environment.

- **Customized Financing Solutions**
  Private credit lenders can structure flexible financing arrangements tailored to borrowers' specific needs. This allows investors to negotiate favorable terms, including higher yields, stronger covenants, and priority in capital structures.

- **Resilience During Market Downturns**
  While public credit markets can be subject to sharp price swings, private credit investments are generally held to maturity and are less susceptible to mark-to-market volatility. As a result, they provide stability even in turbulent economic conditions.

- **Expanding Opportunity Set**
  The growth of middle-market businesses, coupled with the retrenchment of traditional banks from certain lending activities, has expanded the universe of private credit opportunities. Investors are increasingly stepping in to finance these enterprises, filling a critical funding gap.



Historical data highlights private credit's resilience during periods of market stress, such as the Global Financial Crisis and the COVID-19 pandemic. Historically from 2000-2024, upper quartile IRRs have outperformed median IRRs by approximately 800 bps, with upper quartile private debt IRRs at 22%, and median IRRs at 14%. This demonstrates the ability of top-performing private credit funds to deliver equity-like returns with significantly lower risk.

Risks and Challenges

Despite its advantages, private credit is not without risks. Some of the primary concerns include:

- **Liquidity Constraints**
  Private credit investments are inherently illiquid compared to publicly traded bonds, requiring investors to commit capital for extended periods. This necessitates careful liquidity management within a broader investment portfolio.

- **Credit and Default Risk**
  As with any lending activity, private credit carries the risk of borrower default. Proper due diligence, risk assessment, and structuring are essential to mitigate potential losses.

- **Regulatory and Market Uncertainty**
  The evolving regulatory landscape, particularly regarding interest rate policy and financial oversight, could impact private credit markets. Investors must remain vigilant and adaptable to policy shifts.

- **Lack of Market Data**
  Private markets are inherently intransparent and very hard to source reliable market data for investment decision making. This is doubly true for private credit, which was historically a niche strategy and has additional critical metrics to evaluate.

The Future of Public-Private Market Convergence

As traditional public market investors deepen their involvement in private credit, the boundaries between public and private markets continue to blur. This convergence is likely to persist, driven by both cyclical and structural factors. Advances in financial technology, increased institutional expertise in private assets, and growing demand for alternative sources of income will sustain this trend.

Moreover, as the global economy undergoes structural changes—such as rising interest rates, shifting demographic trends, and evolving regulatory frameworks—private credit will remain an essential tool for investors seeking to optimize their risk-return profiles. The growing institutionalization of private credit markets, combined with enhanced transparency and data availability, will further encourage participation from traditional asset managers.

About CEPRES

For over 20 years, CEPRES has served the world's most influential private markets investors by providing them with high quality, granular, private market deal data and world-class portfolio management tools.

Our clients leverage proprietary deal data and complete cash flows from the world's largest private markets ecosystem containing nearly $54T in assets, 141,000+ PE-backed companies, 13,700+ funds, and 6,000 GPs and LPs.*

Through CEPRES' suite of Portfolio Management tools, investors can leverage Predictive Intelligence to forecast portfolio outcomes, conduct rigorous Due Diligence, and identify prospective opportunities using Fund Screener. Additionally, our Portfolio Monitoring platform enables detailed analysis of portfolio composition, facilitating scenario-based forecasting and risk assessment.

When integrated with CEPRES Market Intelligence, investors can construct tailored analyses for the evaluation and modeling of private market strategies, empowering them to anticipate key metrics such as portfolio risk, return potential, projected cash flows, and net asset value (NAV) development with greater assessment.

CEPRES' investment data platform is powered by real-time and predictive analytics so investors can unlock better investment outcomes and make smarter decisions.

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