



A R I N I

Mind the Gap: The Private Credit Premium in the European Non-Sponsor Middle Market

ARINI INSIGHTS PACK

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Principal Insights

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- 1

Europe offers a highly attractive investment environment, particularly with recent shifts in the geopolitical and macroeconomic landscape
- 2

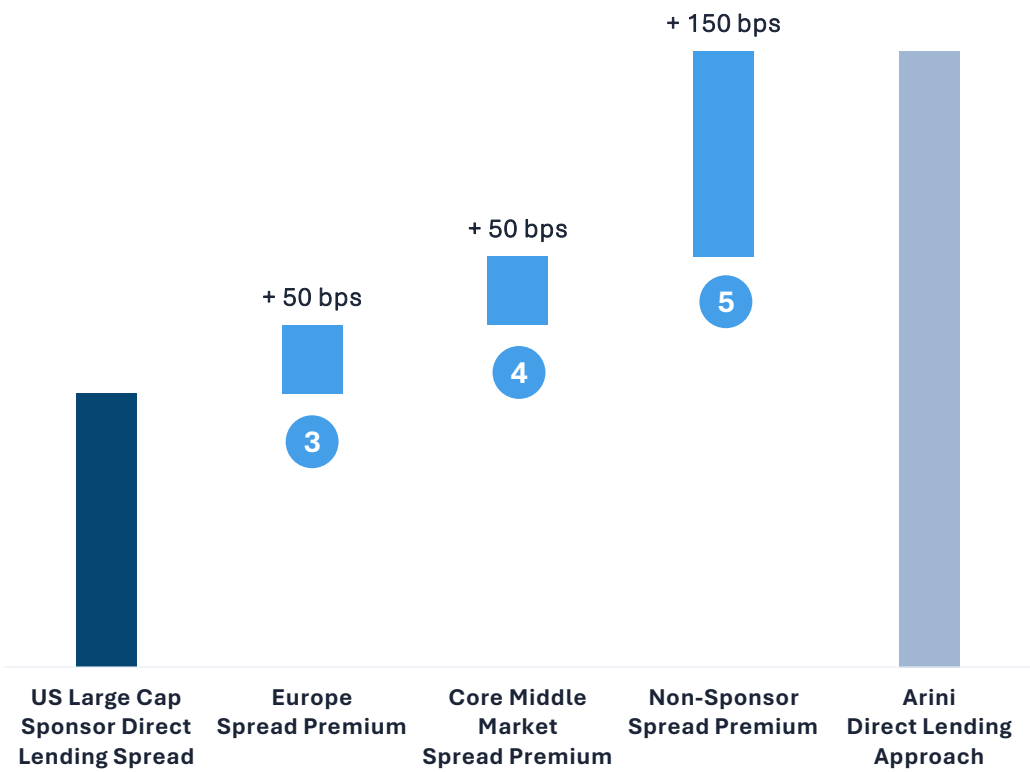
Private credit is integral to driving Europe’s economic agenda, with banks having pulled back from leveraged lending given regulatory constraints
- 3

Direct lending in Europe presents compelling risk/reward to investors relative to the US market and, in particular, when addressed with a balanced approach across sectors and countries
- 4

The core middle market offers higher margins, lower leverage and tighter documentation, especially across the European direct lending landscape
- 5

The non-sponsor opportunity set is deeply underpenetrated in Europe, providing ample white space for direct lenders to partner with multi-generational family-owned companies and generate strong risk-adjusted returns

The European Core Middle Market Non-Sponsor Premium*



* For footnoted information, please refer to footnote 1 on each of page 5, 6 and 7.

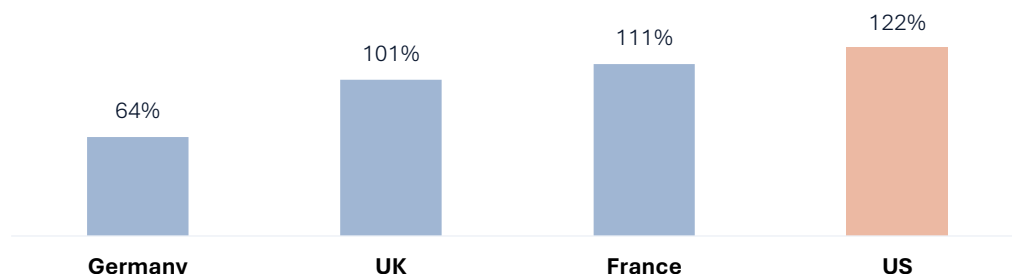
1 Europe offers a highly attractive investment environment

Particularly with recent shifts in the geopolitical and macroeconomic landscape

I Why Europe Today

- a **Europe is experiencing a renaissance as an investment destination**,¹ with geopolitical and macroeconomic shifts reshaping the opportunity set
- b **Major policy initiatives are predicted to recalibrate growth**, including through:
 - The European Commission's Savings and Investments Union initiative and
 - Germany's proposal to create a €500 billion 10-year fund to drive infrastructure investments²
- c **Europe's largest economies are in a more fiscally conservative position** to pursue growth reforms,³ on the back of a more prudent response to the Covid-19 pandemic⁴

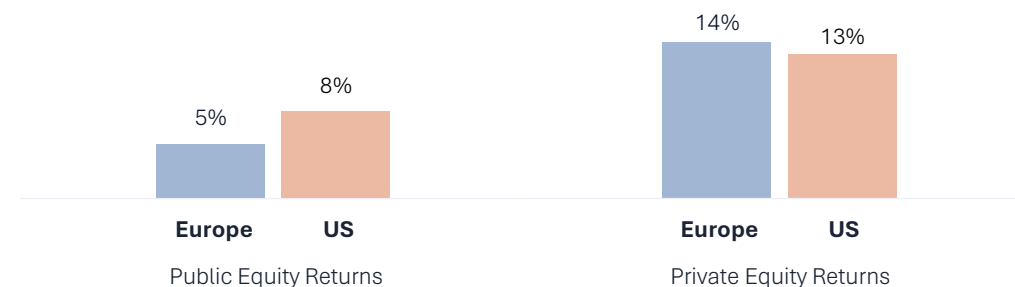
Government debt to GDP lower in Europe's largest economies vs. US (2023)³



II Why Europe, Always

- a **European private capital has outperformed public market equivalents** more often than the US over the past 20 years, and with such outperformance exceeding that of the US by twofold on average⁵
- b **Europe offers abundant opportunity to generate excess risk-adjusted returns** by solving for complexity across the region's various legal, regulatory and political environments
- c The European investment landscape has historically presented diverse and robust opportunity sets to deploy capital over multiple market cycles, **particularly for investors with deep local presence in European credit markets**

Private equity outperformance far greater in Europe vs. US (2000-Q3 2024)⁶



1. Financial Times – KKR says Europe enjoying 'renaissance' after Trump unleashes tariffs (April 2025).

2. Reuters – Key details of Germany's proposed fiscal rule changes, infrastructure splurge (March 2025).

3. IMF, Haver Analytics, with data obtained via Apollo – Rethinking public and private, safe and risky, and passive and active (November 2024).

4. IMF – US and Euro Area Monetary and Fiscal Interactions During the Pandemic: A Structural Analysis (November 2022). Does not include country-specific stimulus.

5. MSCI Burgiss, with data obtained via McKinsey & Company – Private capital: The key to boosting European competitiveness (April 2025).

6. Bloomberg L.P., Cambridge Associates US Private Equity Index and Europe Private Equity Index by S&P Dow Jones Indices (2000-Q3 2024), with data obtained via Davidson Kempner – Europe: Opportunity in Fragmentation (April 2025).

2 Private credit is integral to driving Europe's economic agenda

With banks having pulled back from leveraged lending given regulatory constraints

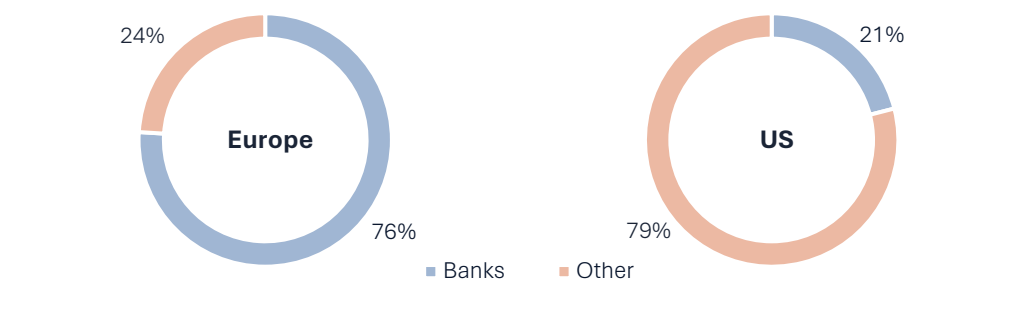
I Bank Financing More Prevalent in Europe versus the US

- a European companies are traditionally more reliant on bank financing,¹ which offers a wider array of corporate financing options to borrowers
- b Bank assets are far larger in size in Europe vs. the US and are even larger when compared to GDP²

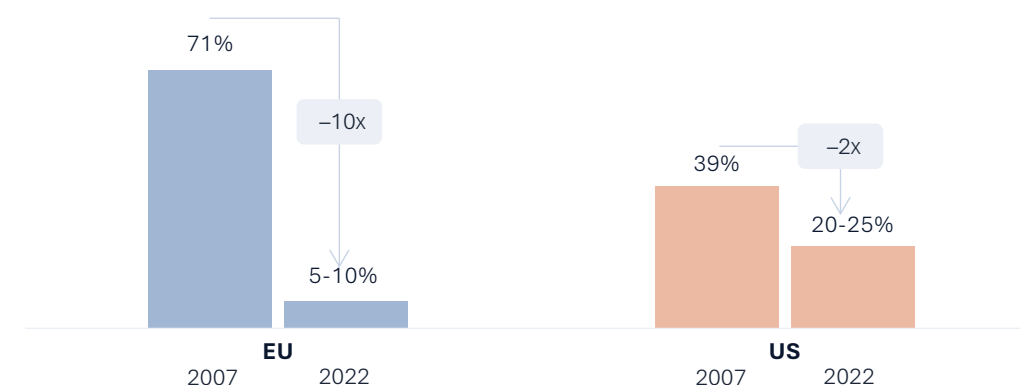
II Yet Banks Reducing Presence in Europe's Middle Market

- a Post-GFC regulations have created a more constrained bank lending environment globally, highlighting the pressing need for private credit to play a meaningful role in financing European businesses
- b Banks have played a decreasing role in leveraged finance in the core middle market, particularly in Europe,³ activity which has been offset, at least in part, by a sixfold increase in direct lending transactions in Europe over the past decade⁴

Sources of financing for the corporate sector Europe vs. US (2024)¹



% of public credit deals <€250m³



1. Pitchbook LCD, Bloomberg, ECB, Apollo Chief Economist, with data obtained via Apollo – The Continental Shift: Europe's Private Credit Moment (June 2025).

2. Federal Reserve Bank of St. Louis (January 2025), Bank Regulatory Reporting (Q4 2024), ECB and EBA (Q2 2024), IMF (December 2024), with data obtained via Apollo – The Continental Shift: Europe's Private Credit Moment (June 2025).

3. Dealogic, LCD, JPM Research, with data obtained via Hayfin – Why Europe? (May 2024). Last 2-year average. Companies with 5x+ leverage and <€250m issuance.

4. Ares Investor Day (May 2024). 2013 to 2023 data.

3 Direct lending in Europe presents compelling risk/reward to investors relative to the US

In particular when addressed with a balanced approach across sectors and countries

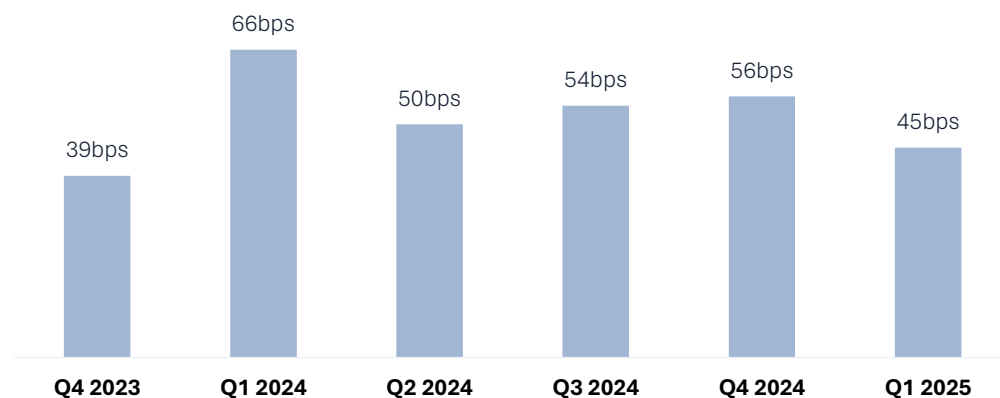
I ~50bps+ avg. excess spread in European direct lending¹

- a Spread premium driven by structural differences between Europe and the US, including a more fragmented market with multiple legal systems and regulatory regimes

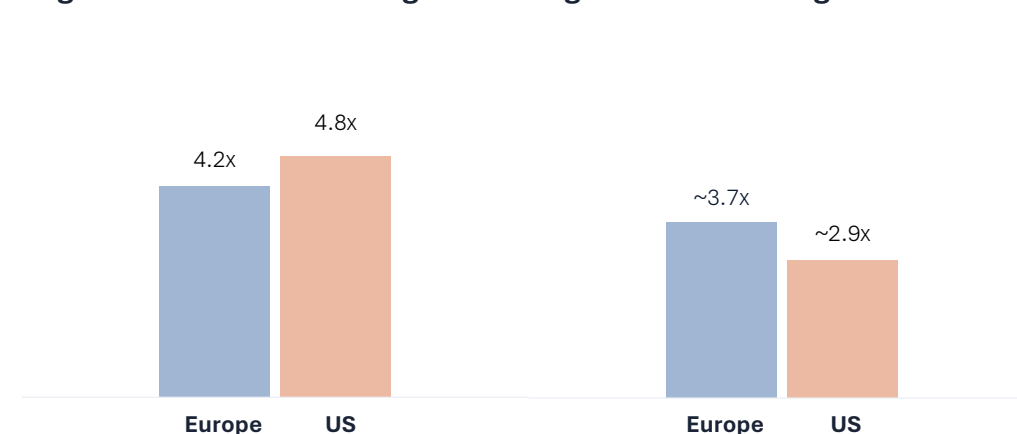
II Attractive credit metrics in European private debt vs. US

- a More conservative leverage and interest coverage ratios in Europe²
- b Market participants might attribute this to an assumed greater proportion of TMT and healthcare deals in the US – sectors often associated with higher leverage – but **the European direct lending market has similar or greater exposure to TMT and healthcare relative to US direct lending³**

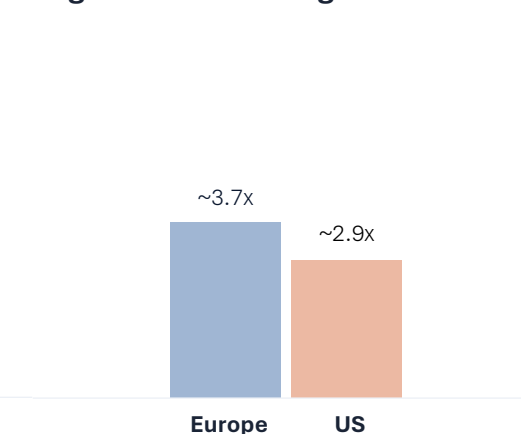
Average excess margin in European direct lending relative to the US¹



Avg. senior secured leverage²



Avg. interest coverage ratio²



1. KBRA, with data obtained via Apollo – The Continental Shift: Europe's Private Credit Moment (June 2025).

2. Preqin 2022 Private Debt Report, with data obtained via Hayfin – Why Europe? (May 2024), and LCD (2010-2023), with data obtained via Goldman Sachs Asset Management – Private Credit's Global Footprint: Opportunity in the Maturing European Market (2024). Interest Coverage Ratio is EBITDA / Cash Interest on LBOs.

3. Deloitte Private Debt Deal Tracker (2019-2024 data), Houlihan Lokey BDC Monitor (Summer 2025). European direct lending represented by transaction count and US BDC data represented by BDC portfolio assets, and Europe.

4 The core middle market offers higher margins, lower leverage & tighter documentation

Especially across the European direct lending landscape

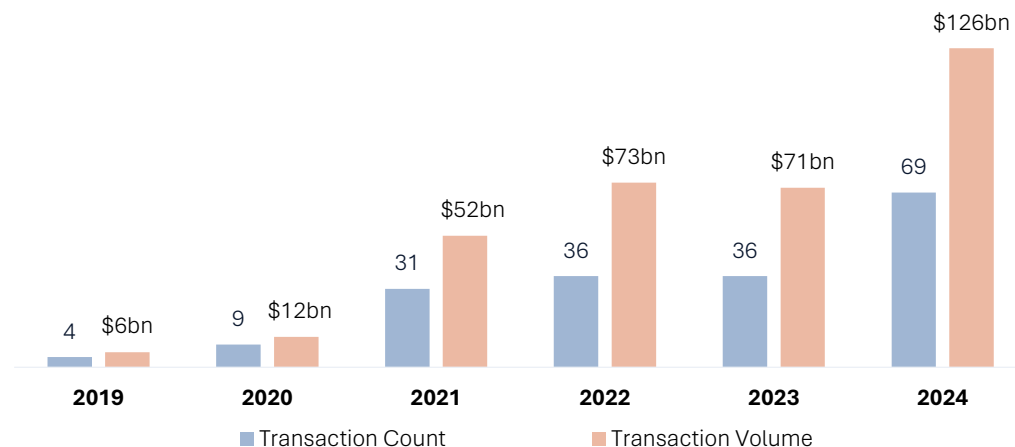
I ~50bps+ avg. excess spread in the core middle market¹

- a Spread premium driven by fund flows into large direct lending transactions (\$1bn+)²
- b Many middle market companies are often insulated from global trade policy headwinds, given their domestically-focused businesses

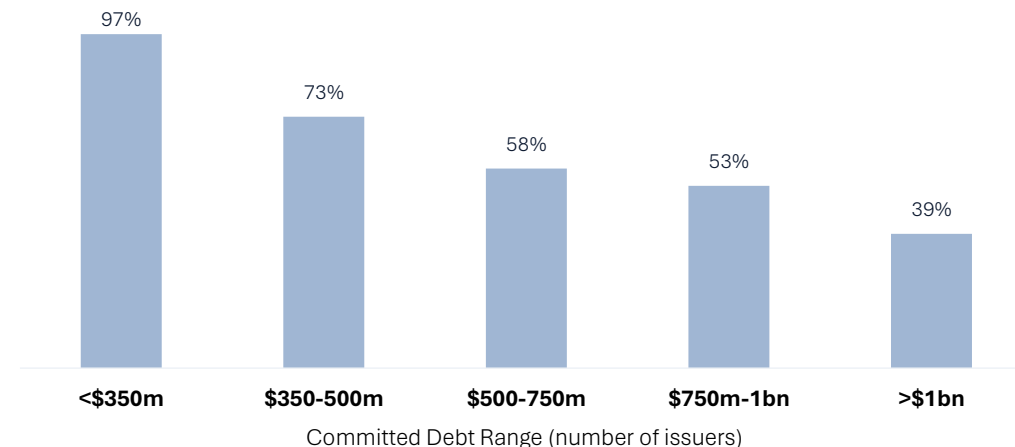
II Attractive credit metrics in the core middle market

- a Leverage levels in the core middle market are typically ~1x lower than larger deals in the upper middle market¹
- b A materially larger proportion of core middle market transactions include maintenance covenants³ – with a far greater percentage of market participants in Europe requiring tighter documentation⁴

\$1 billion+ direct lending transactions²



Presence of maintenance covenants³



1. KBRA DLD Private Data and TPG, with data obtained via TPG – The Advantages of Disciplined Lower Middle Market Direct Lending (October 2024).

2. Arini analysis based on data from KBRA DLD (Direct Lending Deals) modified by data from HPS as of December 2024, with data obtained via BlackRock 2025 Investor Day (June 2025).

3. S&P Global – Documentation, Flexible Structuring Continue to Reign in Private Credit (September 2024).

4. Prequin, Proskauer, JP Morgan Research, with data obtained via Hayfin – Why Europe? (May 2024).

5 The non-sponsor opportunity set is deeply underpenetrated in Europe

Providing ample white space for direct lenders to partner with multi-generational family-owned companies and generate strong risk-adjusted returns

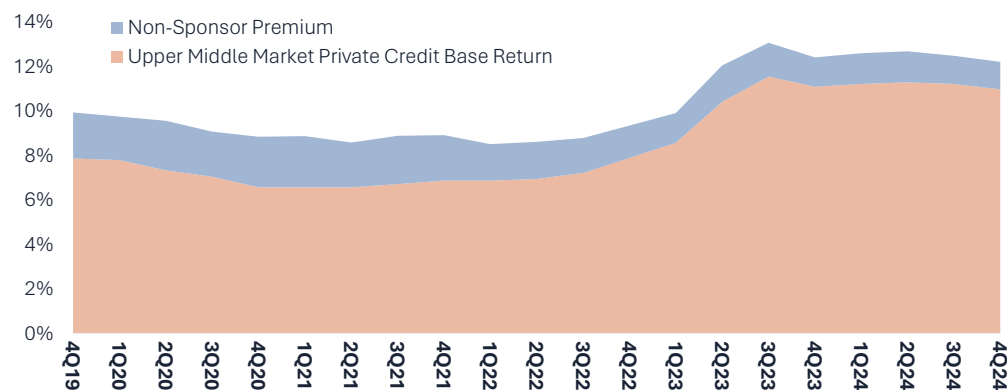
I ~150bps+ avg. excess spread in non-sponsor deals¹

- a Spread premium driven by (a) difficulty originating non-sponsor deals and (b) increased diligence effort – given inability to rely on a sponsor's diligence

II Attractive non-sponsor market penetration opportunity

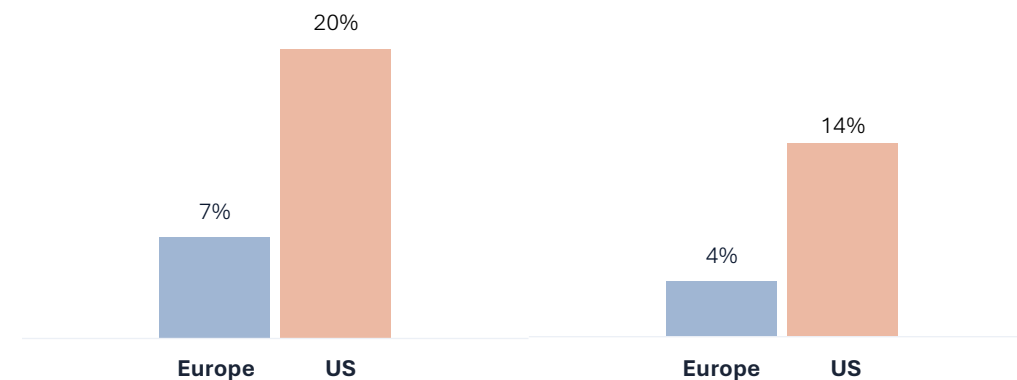
- a Far fewer European companies with \$100m+ in revenue are publicly held vs. the US³ – and yet private equity is far larger in the US⁴ – indicating that **Europe has an even greater proportion of private non-sponsor-owned companies versus the US**
- Despite this, the non-sponsor share of the direct lending market is similar across the US and Europe⁵
- b Non-sponsor share is also meaningfully lower in European direct lending relative to the European high yield bond markets⁶

Industry return premium associated with non-sponsor borrowers²



PE AuM as a % of GDP⁴

% of \$100m+ revenue companies that are public³



1. Average data point from Brookfield - Understanding Private Credit: Sponsor vs Non-sponsored Financing (September 2023), Stepstone - Private Debt Yield Decomposition (July 2023), PGIM - Middle Market Shines in Private Credit (July 2024), Cliffwater - 2022 Q1 Report on U.S. Direct Lending (March 2022).

2. Cliffwater Direct Lending Index, with data obtained via BlackRock 2025 Investor Day (June 2025). Upper Middle Market Private Credit Base Return calculated as the sum of the risk-free rate (T-Bills), the broadly syndicated loan premium (estimated by Cliffwater based on the Morningstar LSTA US Leveraged Loan Index) and the Upper Middle Market Directly Originated Loans premium (estimated by Cliffwater).

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3. S&P Capital IQ, Apollo Chief Economist, with data obtained via Apollo - Rethinking public and private, safe and risky, and passive and active (November 2024). Based on last 12-month revenue.

4. Preqin, Eurostat, Federal Reserve, OECD, DKCM Research, with data obtained via Davidson Kempner - Europe: Opportunity in Fragmentation (April 2025).

5. Arini based on Preqin, Deloitte, with data obtained via Lombard Odier - Widen the net: the case for non-sponsored direct lending exposure (April 2024).

6. Deloitte Private Debt Deal Tracker (reports with H2 2019-H1 2023 data), PitchBook LCD European Credit Markets Quarterly Wrap (July 2023). Based on direct lending transaction count and High Yield issuance volume.

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