ALPINVEST

CARLYLE | GLOBAL INVESTMENT SOLUTIONS

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Beyond NAV Lending

Portfolio Finance 2.0: Accelerating Credit Solutions for Private Capital

Key Takeaways

1. This study provides an update of a White Paper we issued in November 2021. Several factors warrant a fresh look at *Portfolio Finance*. Most importantly, our initial projection of the significant growth of this emerging asset class appears to have proven conservative in subsequent market developments.

2. Against this background, we provide a revised medium-term scenario, according to which deal volume could increase to almost **$100 billion by 2028**, limited only by the availability of capital for these financings.

3. We estimate that Portfolio Finance transactions totaled **$22 billion in 2023** across fund financings, LP interest financings and GP financings, representing a more than sevenfold increase since 2019.

4. Since the publication of our initial White Paper, adoption of portfolio finance has increased considerably faster than we had anticipated. We explore the causes for this acceleration in the growth of Portfolio Finance, including the liquidity issues that have been caused by the unanticipated increase in interest rates in 2022 – 2023.

5. While Limited Partners (LPs) and General Partners (GPs) alike have sought efficient solutions to address these liquidity issues, the dramatic shift in the global interest rate environment has laid bare that equity-based instruments may not always be the preferred choice. Instead, credit-based solutions may be more efficient in certain situations.

6. While the emergence of liquidity constraints amid a surge in interest rates has served as a catalyst for Portfolio Finance, we believe that the market will continue to see robust growth over the medium term.

7. Notwithstanding the sharp increase in deal activity over the past four years, we believe that the Portfolio Finance market is still embryonic. Rather than view the recent surge in deal volume as a cyclical phenomenon, we anticipate the accelerated usage of these solutions to improve awareness and adoption among GPs and LPs of more flexible solutions in fund financings, LP interest financings and GP financings.

8. In discussing this outlook, we emphasize the flexibility of Portfolio Finance, encompassing a range of instruments, including traditional loans and preferred equity (which we further segment into unitranche, mezzanine and structured equity). These structures, which can be tailored to the specific needs of GPs and LPs, may complement existing equity-based options.

9. As part of the evolution of the GP centered secondaries market we are seeing sponsors use credit-oriented NAV-based instruments. Fund financings may be preferred when funds seek to recapitalize portfolio companies, require capital for growth investments and opportunistic acquisitions, or wish to increase the liquidity position of their holdings without selling or diluting exposure in the underlying assets especially if buyers cannot agree on the GP's valuation.

10. Informally described as the **intersection of private credit and secondaries**, we believe Portfolio Finance is emerging as an asset class with distinct risk-return properties, including cross-collateralization of underlying assets, cash flow priority and meaningful asset over-collateralization.

11. Market conditions are anticipated to remain favorable as adoption by issuers of Portfolio Finance increases, consistent with comparable developments in the private equity secondary market.

12. Overall, we believe that Portfolio Finance has the potential to play an increasingly important role in investors' portfolios, just as private credit has evolved as an investment strategy over the past decade.

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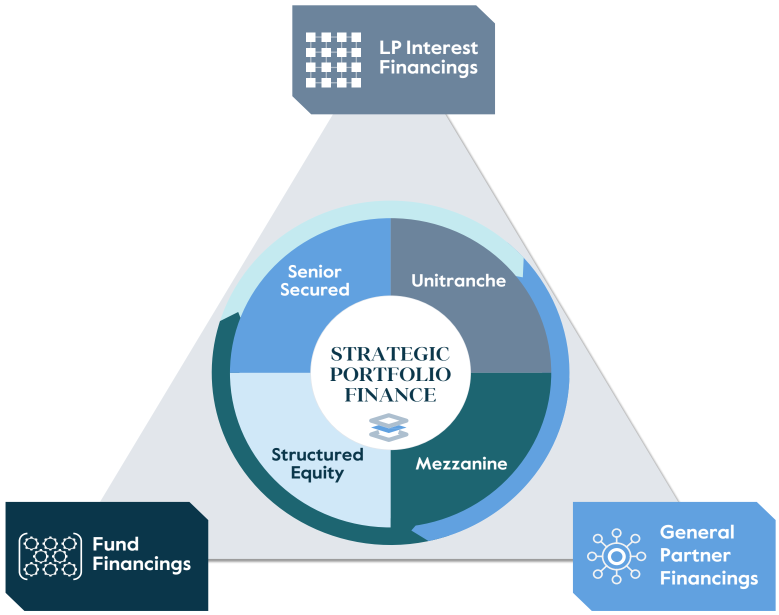

For illustrative purposes only.

AlpInvest believes that the Portfolio Finance market is best understood by bringing together three closely related financings; (i) **Fund Financings** also often referred to as **NAV lending**; (ii) **GP Financings** that relate to the assets of a fund manager and (iii) LP Interest Financings involving portfolios of interests in private funds.

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