EXPERT Q&A

Mattis Poetter of Arcmont Asset Management and Mat Linett of Churchill Asset Management explain why the picture for mid-market lending remains compelling, despite negative headlines

Focus on the fundamentals

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Q There's a growing narrative around risks in private credit. How do the headlines stand up to what you're seeing?

Mat Linett: There's a real disconnect between current private credit fundamentals and what's dominating the headlines. We lend to core mid-market companies in the US – typically with $10 million-$100 million in EBITDA – and we're continuing to see both organic and inorganic growth across our portfolio, with industry default rates remaining exceptionally low.

Much of the noise tends to centre on retail participation, which underscores the need for greater investor education around liquidity, risk and what to realistically expect from private credit. Many entering the space are doing so for the first time, and some degree of market recalibration is a natural part of that maturation process.

Defaults and losses will occur in any credit cycle – that's to be expected. But the fundamentals remain sound, and the risk-adjusted returns on offer should provide meaningful cushion to absorb any losses while still delivering compelling outcomes for investors.

Q How is AI disruption affecting direct lending?

Mattis Poetter: We started working with an external AI consultant a couple of years ago to screen our portfolio and flag potential risks. Everyone talks about software as a target for AI disruption, but in our view, effective risk management goes well beyond this specific sector; you have to screen your entire portfolio.

We believe ours remains in really good shape, but this was driven by credit decisions we made long before AI entered the mainstream media, because we've always wanted to invest in strong, market-leading companies. We're incorporating AI into every single investment memo and due diligence process we launch in order to build a portfolio that should be able to weather any of the pressures brought on by further AI development.

ML: AI won't disrupt every industry for the worse, but our goal is to avoid binary outcomes. When we believe

an industry is at an inflection point, staying ahead of it matters – pursuing sound underwriting principles, working with strong sponsors, maintaining diversification by attachment point and always preserving a margin for error.

Q How are the Iran war, inflation, supply chain pressures and oil prices impacting your outlook, and do you expect a recession?

ML: The nice thing about private markets is that you're anchored to fundamentals, and fundamentals don't change with the news cycle. We focus on service-orientated businesses with strong recurring cashflows, market-leading positions and the pricing power to pass through cost increases.

Uncertainty also creates opportunity for well-capitalised, patient investors. Spreads have widened 25-50 basis points in many cases, documentation has strengthened, and as some BDCs face redemption pressures and pull back, dealflow in the core mid-market is increasing. That creates room for managers with primarily institutional capital and consistent origination to step in.

Recession or not, portfolios that are grounded in strong credit fundamentals are well positioned to navigate what's ahead. We underwrite every single loan with recession top of mind at some point during our hold – structures need to be crafted with that in mind and the ultimate impact to our cashflows.

Q How has the current market environment affected dealflow, pricing and terms, and what do you expect for the rest of the year?

MP: In our view, it's a great deal environment. Last year, liquid markets were strong in Europe. The US funds that have been handling retail redemptions have had plenty of liquidity so they would also invest in Europe. But that has gone, so for now, these funds have largely left the scene.

The liquid markets are also volatile, and that's great for the large players who have good balance sheets and scaled funds, because we can look away from the public perception and market volatility through to the fundamentals. We see an opportunity to take the same risk you took last year with better pricing potential, less leverage and stronger documentation.

Q Will direct lending remain the backbone of private credit? What other strategies are you finding interesting right now?

ML: Direct lending remains the cornerstone of private credit – scalable by nature and deeply embedded in serving the private equity ecosystem, alongside adjacent strategies like junior capital that broaden the capital stack. Even as other strategies gain momentum, market innovations will continue to build around it.

Two other areas we're finding particularly interesting today are capital solutions and credit secondaries. Both offer a degree of flexibility that is difficult to find elsewhere, as well as countercyclical benefits – whether it's structuring creative financing solutions for complex situations or accessing seasoned portfolios at compelling entry points.

MP: The European private credit market is still only a fraction of the size of the US – we have at least five to 10 years of growth ahead of us before catching up. Impact lending strategies have really taken off in Europe, particularly among Nordic and Benelux investors. Fund finance is also attracting a lot more LP interest.

Q How do you see the industry evolving over the next five to 10 years, and what will be the biggest areas of growth?

MP: Over the last five years, you've seen the top five European managers consolidate their power and pull ahead of everyone else, because in our view the largest managers are more likely to offer diversified products to investors. Less experienced managers often don't diversify enough.

ML: Two growth areas stand out. First, the continued and deepening interest from the insurance community. Second, private wealth – an opportunity that isn't going away regardless of the current environment. Individual investors remain meaningfully underallocated, and a truly balanced portfolio means including assets that behave differently from traditional stocks and bonds. As those allocations grow, education will be essential to ensuring the decisions behind them are thoughtful and built to last.

Q What do you specifically see for the mid-market's evolution?

ML: The US mid-market is, on a standalone basis, one of the top five largest economies in the world – yet the number of firms that can meaningfully compete here is naturally limited. It's a relationship- and club-driven environment, not a transactional one.

While the lower mid-market is more accessible, the core mid-market is a different proposition. A $50 million EBITDA company, for example, requires five turns of debt – meaning you need to underwrite $350 million to $400 million in a single name including unfunded requirements. That scale requirement alone narrows the field considerably.

Compare this to public markets, where the number of listed companies has been cut in half since 2000. The mid-market continues to be a hotbed of innovation and opportunity, which we believe should continue to create compelling opportunities for investors. ■

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