

Advisors Manual

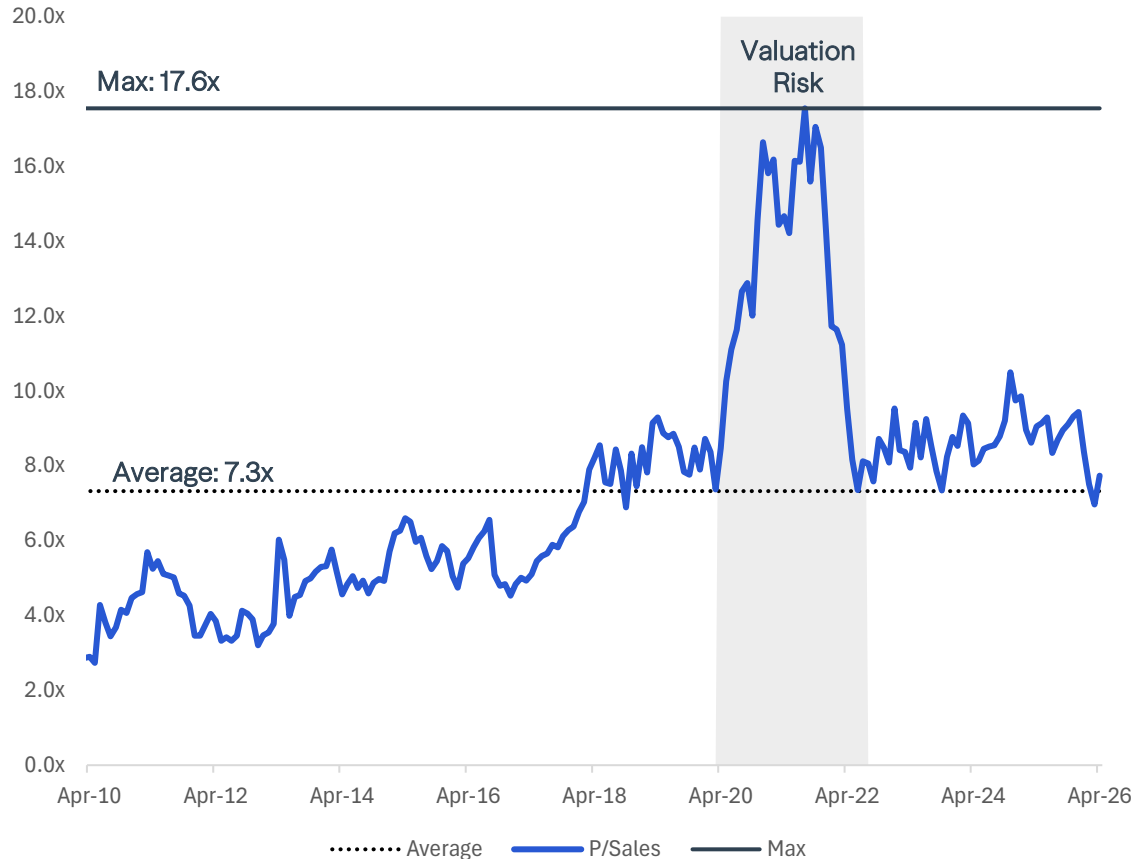
How to Track “Problem Investments” Across
Private Credit and Equity

May 2026



• Software is a primary source of vintage risk in the private markets

Premium valuations in 2020 to 2022 are a reason for vintage valuation risk
Price to sales ratio for the software sector (April 2010 – April 2026)



Private market funds that invested in software are facing two concerns:

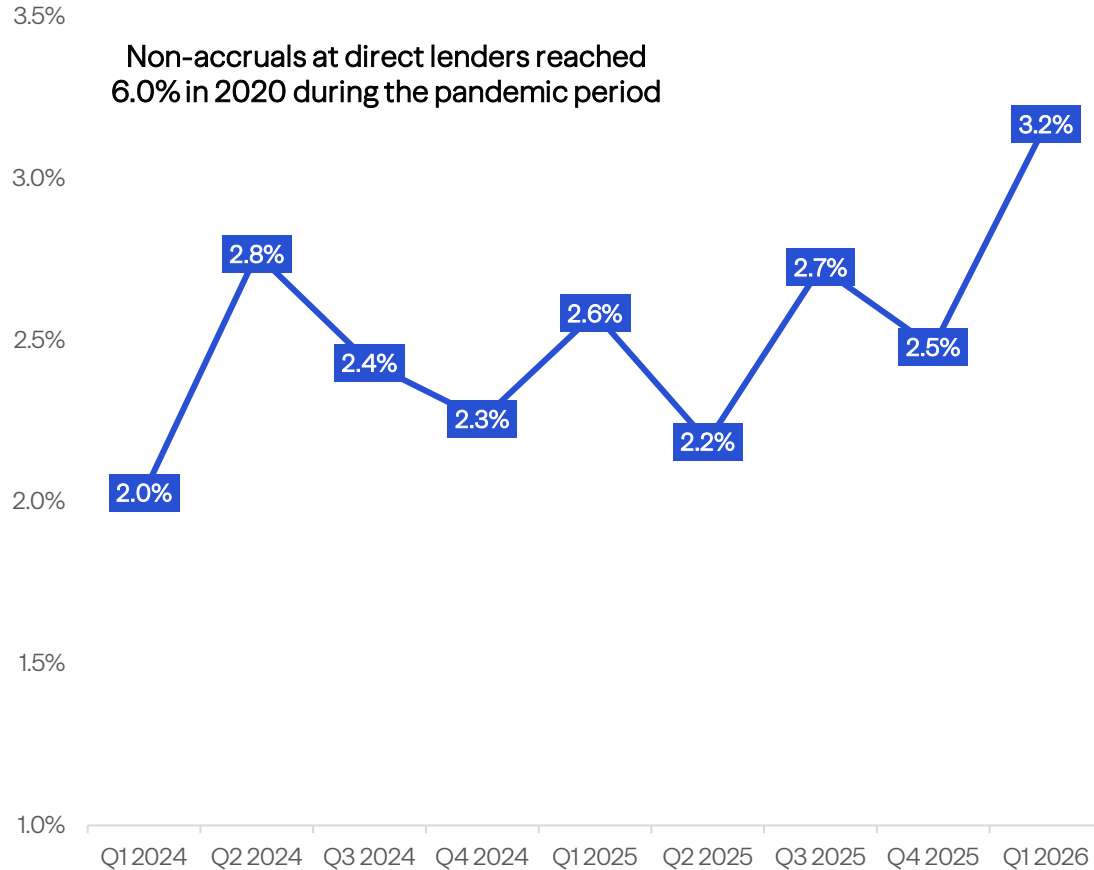
1. **Valuation risk:** Certain credits have always had vintage valuation risk—those transactions that were underwritten at peak valuations.
2. **Operating risk:** AI has introduced uncertainty to the viability and forward growth of the sector.

The sharp valuation correction is a sticking point for managers looking to exit software investments and in having confidence in future valuations.

Source: Bloomberg, as of April 30, 2026. Software sector is proxied by index members of the IGV software ETF as of April 2026. Price to sales ratio is based on trailing 12-month revenue. Data is subject to change as final data is reported. For illustrative purposes only. Past performance is not indicative of future results. Future results are not guaranteed.

Private credit loan books are again starting to reflect credit concerns

Loans on non-accrual status ticked up in Q1 2026 (publicly traded BDCs)
Loans on non-accrual status as a percent of the total investment portfolio (amortized cost)



Credit quality concerns are starting to appear with credit funds placing more loans on non-accrual status. Q1 2026 non-accruals increased 70 basis points (bps), or about 10%, and are up over 100 bps over the last two years.

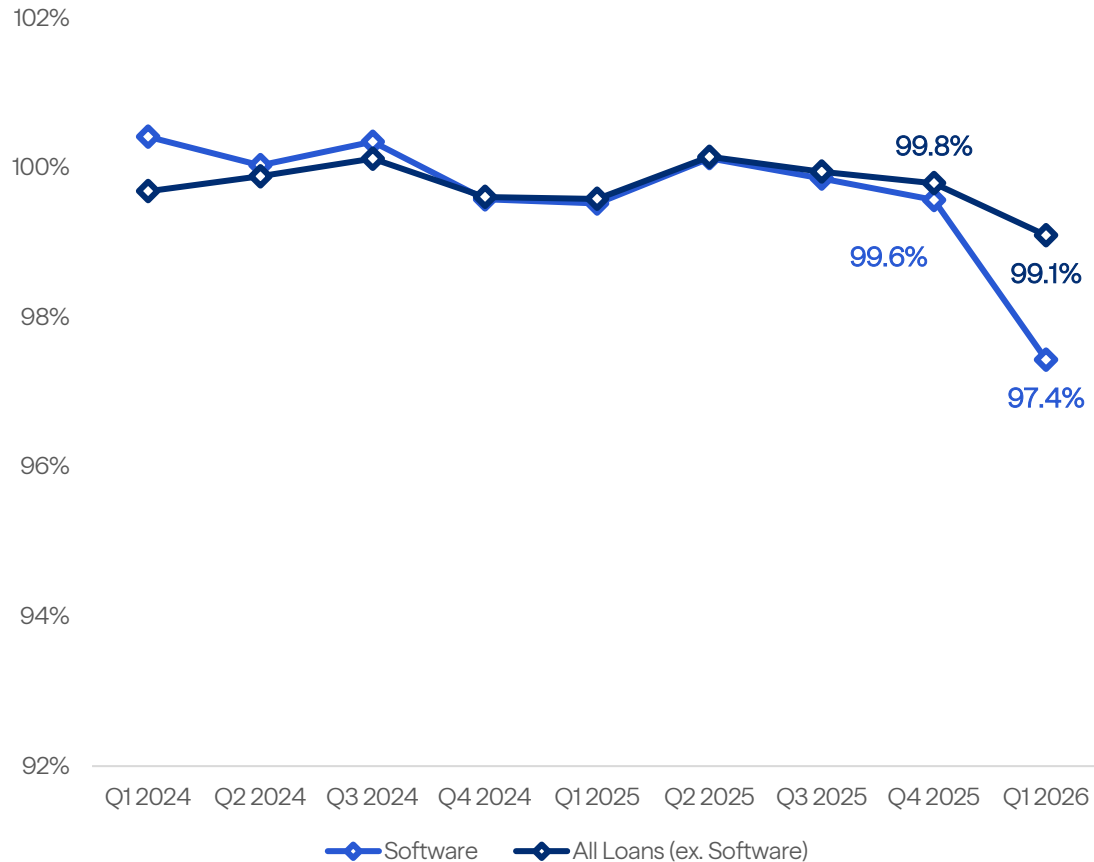
Non-accruals are a proxy for loans that are more likely to generate realized losses.

Loans that were made at peak valuations—where valuation compression has hit the hardest—are one reason for the uptick in non-accruals.

Source: Bloomberg, company filings. Note: data is from public BDCs in the S&P BDC Index that have reported March 2026 results, as of May 8, 2026. Note: A basis point (bps) is a hundredth of 1%. Data is subject to change as final data is reported. For illustrative purposes only. Past performance is not indicative of future results. Future results are not guaranteed.

• Fair values of private credit loan portfolios have also been marked down

Aggregate loan marks for the largest private credit funds: software vs. total portfolio
Loan marks reflect the ratio of fair value to loan cost



Another indicator of private credit performance is the fair value of the underlying loans. Software seen the more drastic fair value markdowns with portfolios now marked at 97.4%, a 214 bps reduction from December 2025.

Importantly, markdowns don't always reflect credit quality or indicate a loss will occur. A private credit manager can markdown a healthy credit simply because market rates, or the spread of newly originated loans, has changed.


For example, a lender that originated a loan at SOFR + 500 a year ago could mark down that loan if a comparable new loan is originated at SOFR +550.

Source: SEC filings, iCapital analysis as of May 13, 2026. Note: data is from the 12 largest non-traded BDCs by net assets. Software categorization is defined by each fund. Data is subject to change as final data is reported. For illustrative purposes only. Past performance is not indicative of future results. Future results are not guaranteed.

• What does this mean for credit quality and performance?

Non-accruals and fair value marks are different measures and reflect different risks. The process to determine fair value includes:

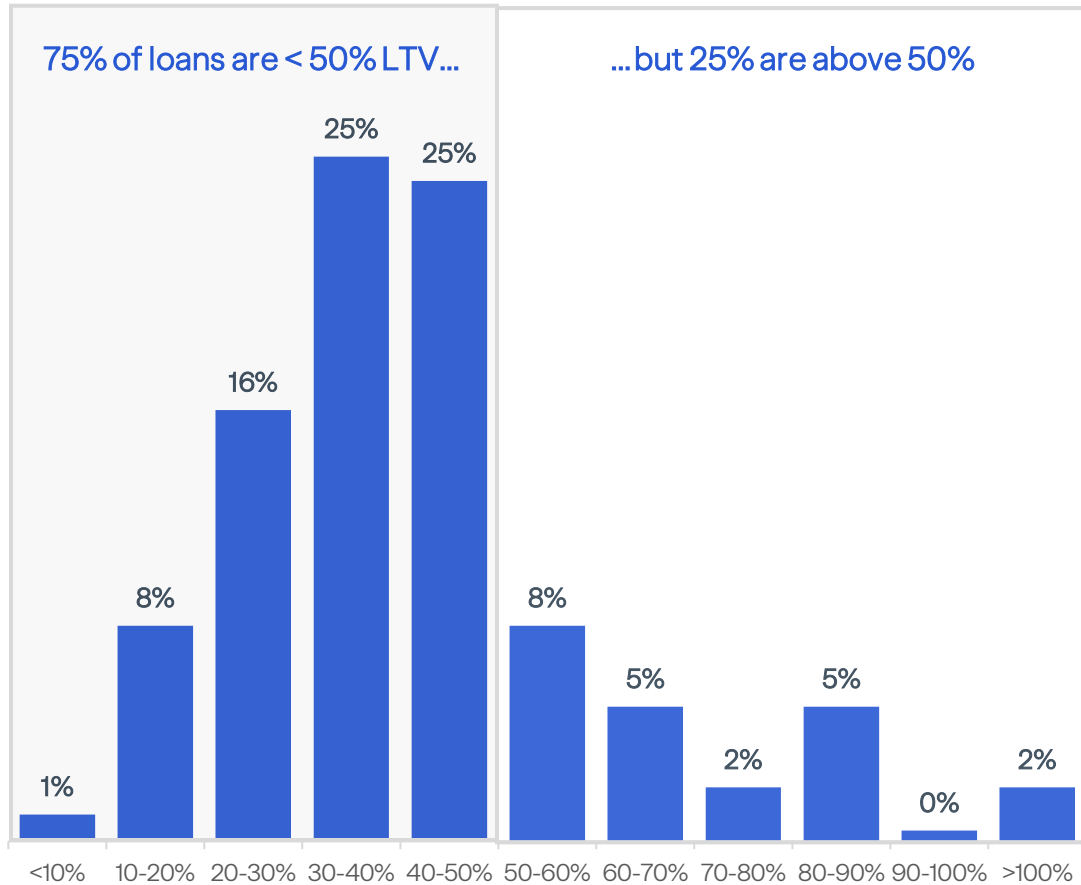
- **Pricing inputs** reflects the return component. Loan prices are adjusted to reflect the current return needed for the risk of the investment. For example, if spreads on newly originated deals widen, the loans prices in the portfolio are marked down to reflect the required return to compensate for the newly priced risk.
- **Credit inputs** focus on the likelihood of getting back the original investment. A loan is marked down if there is a higher probability that the loan principal will not be repaid.



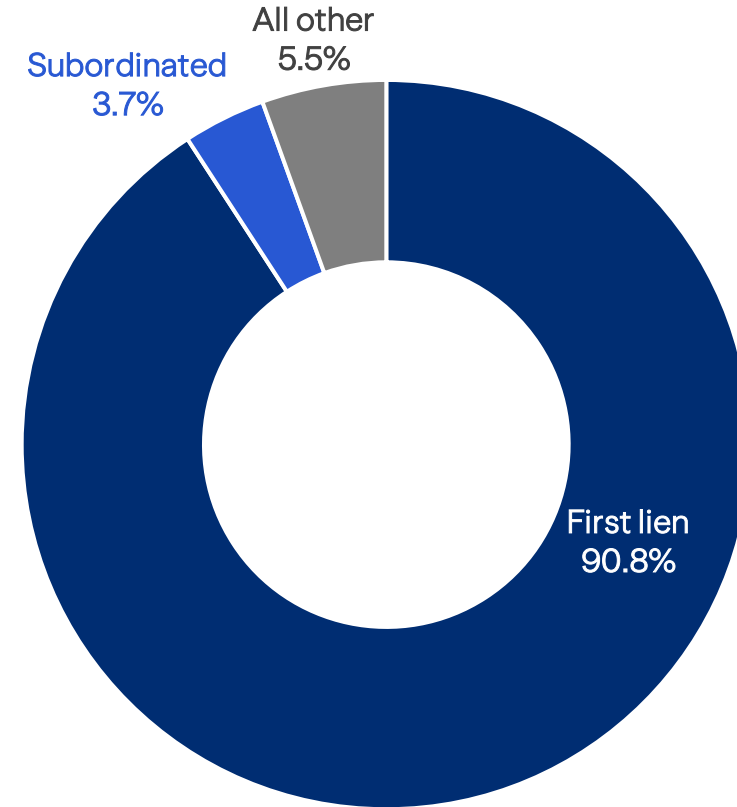
Q1 2026 revisions in fair value marks reflect **downward revisions in pricing inputs** and select credit inputs, primarily with software credits.

• Even with credit concerns, the portfolio is lower-risk and has protections

75% of software borrowers have loan-to-value (LTV) ratios below 50%
LTV distribution for direct loans: software sector



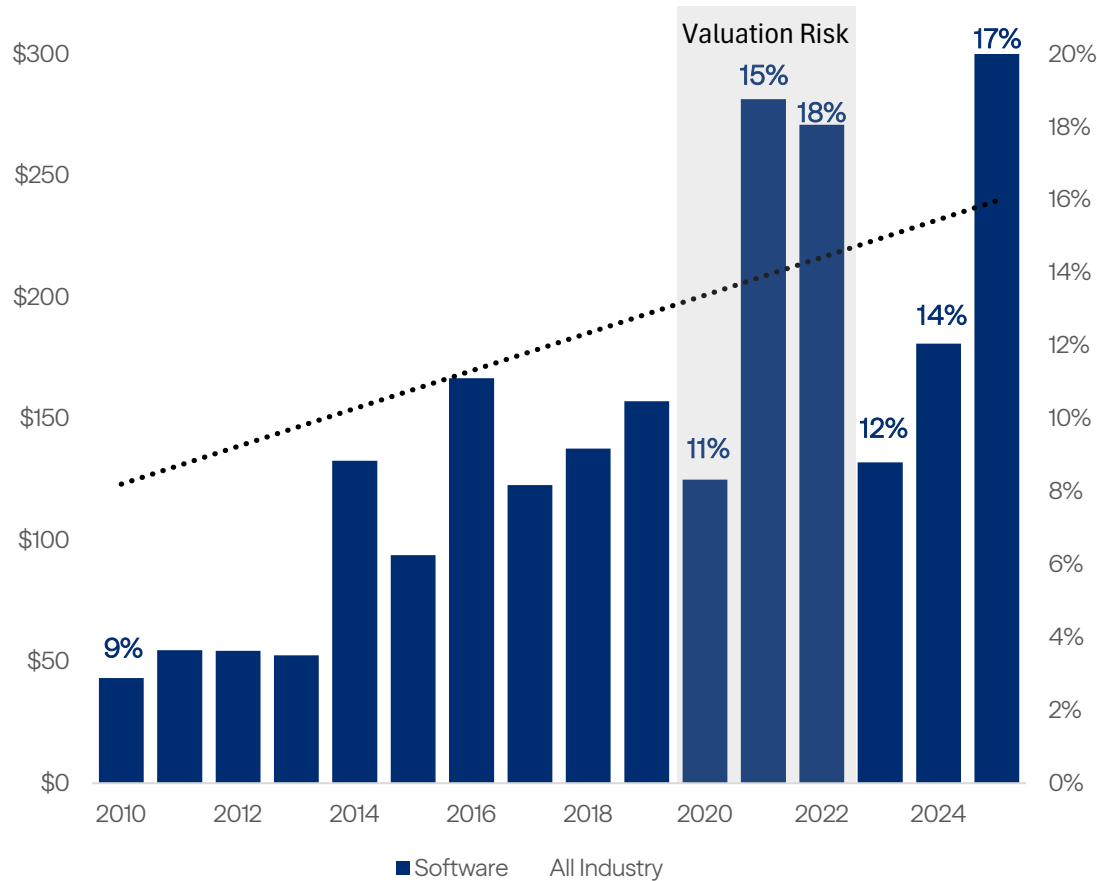
Software investments held by private credit funds are largely first lien
Portfolio composition for software investments held at the largest private credit funds



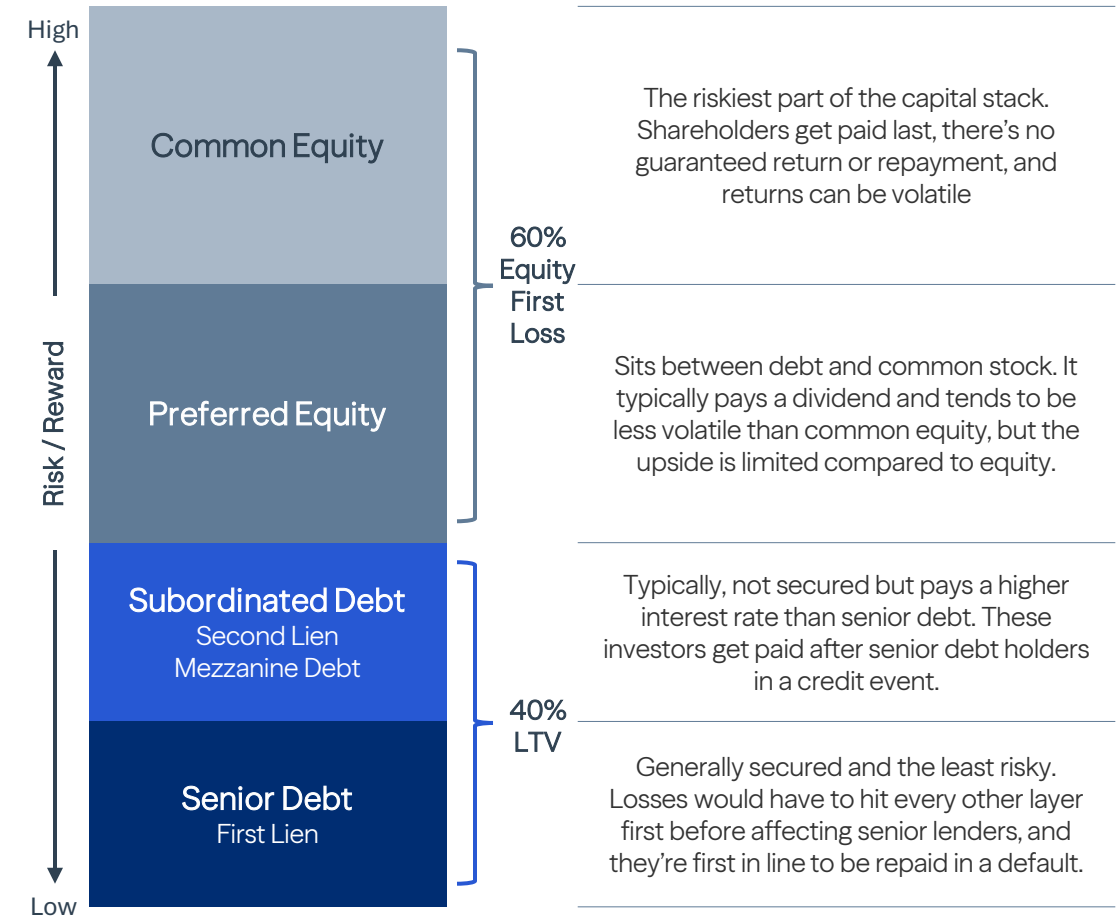
Source: (LHS) Houlihan Lokey Private Credit Databank, Q425 Market Trends and Insights, dated March 2026. (RHS) Software investment categorization across the 12 largest non-traded BDCs measured by net assets, as of May 2026. All other included equity and unclassified. For illustrative purposes only. Past performance is not indicative of future results. Future results are not guaranteed.

• The equity side has fewer protection features and is generally first loss

Since 2010, software has become a larger piece of private equity portfolios
Private equity capital deployment in software and as a percent of total portfolio (\$ in billion)



For problem loans, material losses would occur to the equity before credit
A generic capital structure with 40% LTV, average for sponsor-based software company loans

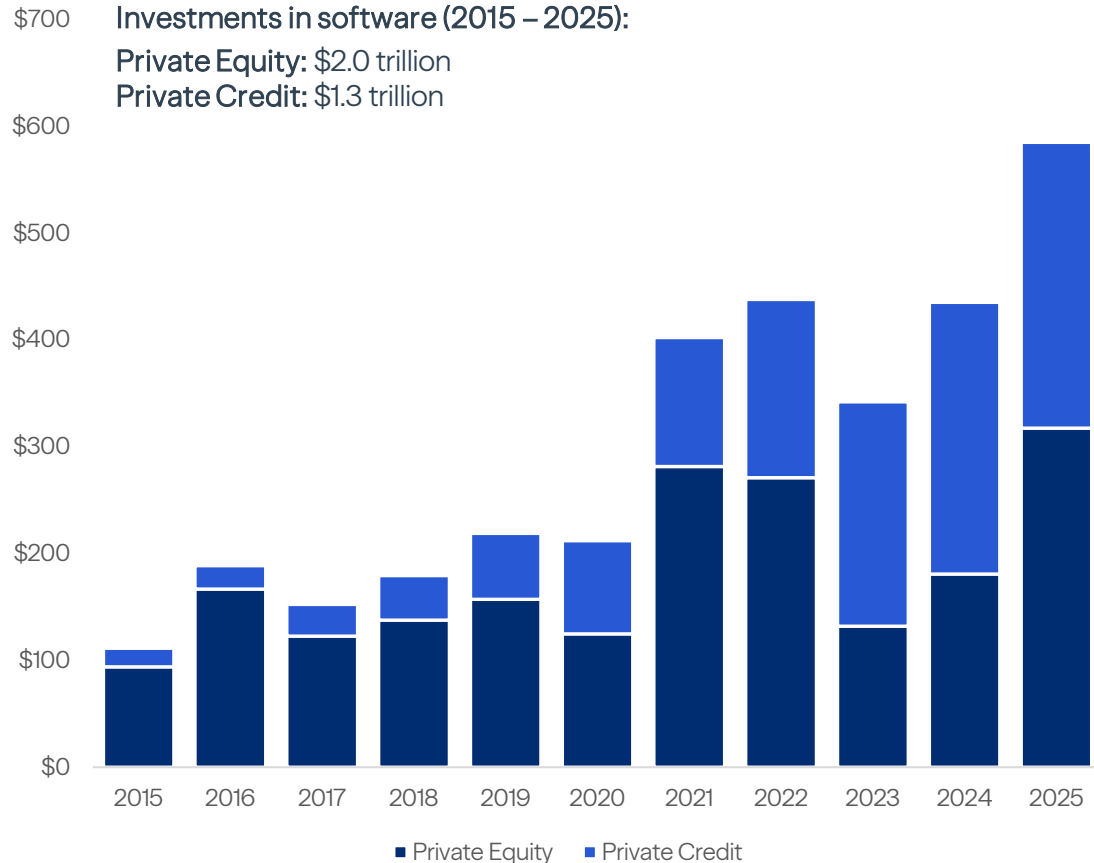


Source: Pitchbook, May 2026. Note: Data is through December 2025. Software is proxied by industry definitions provided by PitchBook. Data is subject to change. For illustrative purposes only. Past performance is not indicative of future results. Future results are not guaranteed.

Private equity capital in software is nearly 2x that of private software debt

For all the private credit software debt, PE has invested nearly double in these companies

Private equity and private credit capital invested in software (\$ billion, except where stated)



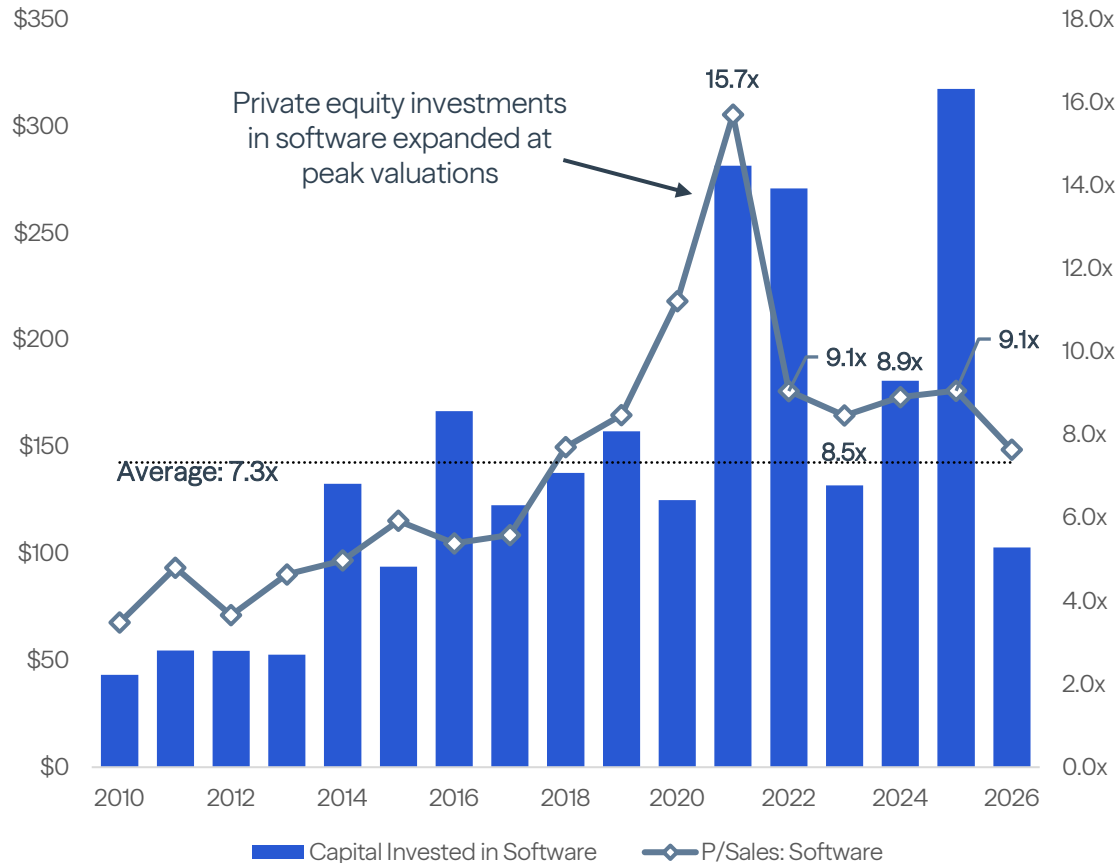
Private equity and private credit have a symbiotic relationship – many PE sponsor-based deals are underwritten with private credit.

Private software debt is the smaller and more senior piece. **Meaning,** for all the private credit in software, there is almost 2x private equity invested in these companies.

Source: PitchBook, Preqin, Barclays Research and iCapital analysis, as of May 2026. Private equity is measured by all private equity buyout capital invested in software. Private capital is measured by capital invested by BDC and direct lending drawdown funds invested in software. For illustrative purposes only. Past performance is not indicative of future results. Future results are not guaranteed.

Concentration of peak valuations deals can lead to performance issues

Private equity investments at peak valuations are bound to produce losses
 Private equity capital deployment and average P/Sales valuation of software (\$ billion)



Transactions in the 2020-2022 era, done at 10x to 18x revenue, can be the vintage risk assets. There is not a clear exit path for these investments as widespread valuation compression is a sticking point, leading to longer holding periods.

If a private equity manager needs a realization or liquidity, it can crystallize losses. But there will be a cohort of companies that adapt. They will adjust to the agentic era, change business models and could see valuation expansion. There will also be others that don't

It's important to remember that there will be software winners. Here, private equity has all the upside exposure.

Source: Bloomberg, PitchBook as of April 30, 2026. Software sector valuation is proxied by index members of the IGV software ETF as of April 2026. Software sector capital invested is proxied by industry definitions provided by PitchBook. Price to sales ratio is based on trailing 12-month revenue. For illustrative purposes only. Past performance is not indicative of future results. Future results are not guaranteed.

• Equity and credit markets are not responding the same way to concerns

Private market investments should be looked at differently due to different objectives

Credit

Private credit managers goal is to avoid loss.

Portfolios that consistently avoid losses will be top performers while performance of lower tier funds are undermined by losses. Lenders cannot offset losses with excess return, or alpha.

Loan mark downs due to pricing risk are unrealized, or paper losses. Non-accruals signal a more likely loss.

Equity

Private equity investments will have successful and unsuccessful investments. Managers can be successful with both outcomes in a well-diversified portfolio.

Equity managers rely on alpha generation. Consequently, software assets can be good “credit assets” while at the same time be much more uncertain “equity assets”.

— • A framework for evaluating problem investments

Workstream	For the loans placed on non-accrual status or have been marked down	For private equity investments financed with private credit that are under pressure
<p>Diagnose the issue</p>	<ul style="list-style-type: none"> • Why was the loan placed on non-accrual? • For marked-down loans, how much of the change reflects market pricing versus borrower fundamentals? 	<ul style="list-style-type: none"> • What factors are driving the current pressure on the investment?
<p>Assess the severity</p>	<ul style="list-style-type: none"> • What is the weight of this investment in the portfolio (available in filings for most credit funds)? • What is the expected recovery outcome? • For markdowns driven by underperformance, how was fair value determined and has the valuation methodology changed? Note that distressed loans can be marked across a much wider range (0% to about 80% of cost) versus performing loans (typically 95% to 100%) • What is the expected outcome for the investment? 	<ul style="list-style-type: none"> • What is the position size within the portfolio? • How have the enterprise value multiples used in the valuation changed since the original investment? For a software investment, you should expect the manager to be using a lower multiple today than when the deal was closed. • What is the expected holding period, and exit path? • Is the company in compliance with its lenders?
<p>Evaluate manager response</p>	<ul style="list-style-type: none"> • What actions are being taken to stabilize or recover value? These may include forbearance (wait and see), restructuring (in or out of court, contentious or consensual), or a sale of the company. 	<ul style="list-style-type: none"> • What operational improvement or value creation initiatives are underway?

Important Information

INDEX DEFINITIONS

IGV iShares Expanded Tech-Software Sector ETF: The iShares Expanded Tech-Software Sector ETF seeks to track the investment results of an index composed of North American equities in the software industry and select North American equities from interactive home entertainment and interactive media and services industries.

S&P BDC Index: The S&P BDC Index is designed to track leading business development companies that trade on major U.S. exchanges.

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