CVC

CVC Credit Perspectives

Attractive opportunities across global credit

Q3 2024

Marketing Material

For Professional / Institutional Investors only - not for Retail use or distribution

Market update

Macro Update:

- Risk asset classes continue to perform strongly as markets become increasingly optimistic that a soft landing is possible (p.1)
- The US economic outlook appears more mixed, and the future direction of the country, both economically and politically, could turn on a dime depending on the election outcome (p.2)
- The European macro outlook remains challenged, with traditional stalwarts such as France and Germany faltering. In the UK all eyes have switched to the Budget which will be a crucial litmus test for the new Labour government (p.2)

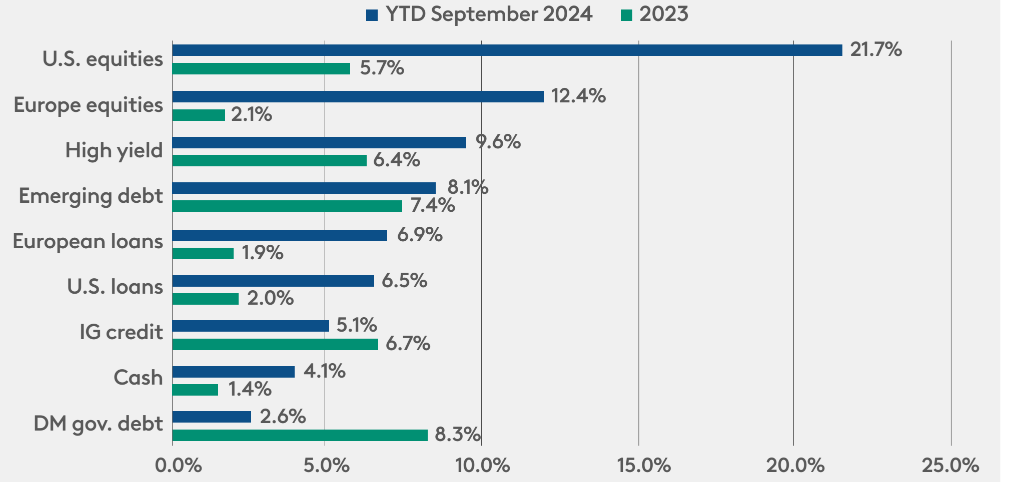
Liquid Credit Markets:

- High yield spreads continue to grind tighter, with the US continuing to trade tighter than Europe (p.3)
- Default rates remain benign, although credit deterioration is evident (p.4)
- High yield and leveraged loan issuance remains strong, although demand outstrips supply (p.4)
- CLO activity has been very strong in 2024, with equity investors being particular beneficiaries due to high Reset and Refinancing volumes, driving higher distributions (p.4/5)

Private Credit Markets:

- Spreads have compressed as a result of a resumption in broadly syndicated loan ("BSL") activity (p.6)
- Middle-market lenders have pivoted back to their core-focus as larger issuers turn to the public markets for refinancing (p.7)
- Interest rate cuts are spurring M&A activity on, meaning the private credit pipeline remains very strong as sponsors look for flexible and reliable financing solutions (p.7)
- There has been some limited cases of credit deterioration, but underwriting remains conservative and European private assets continue to perform strongly (p.7)

Exhibit 1
Performance Across Asset Classes

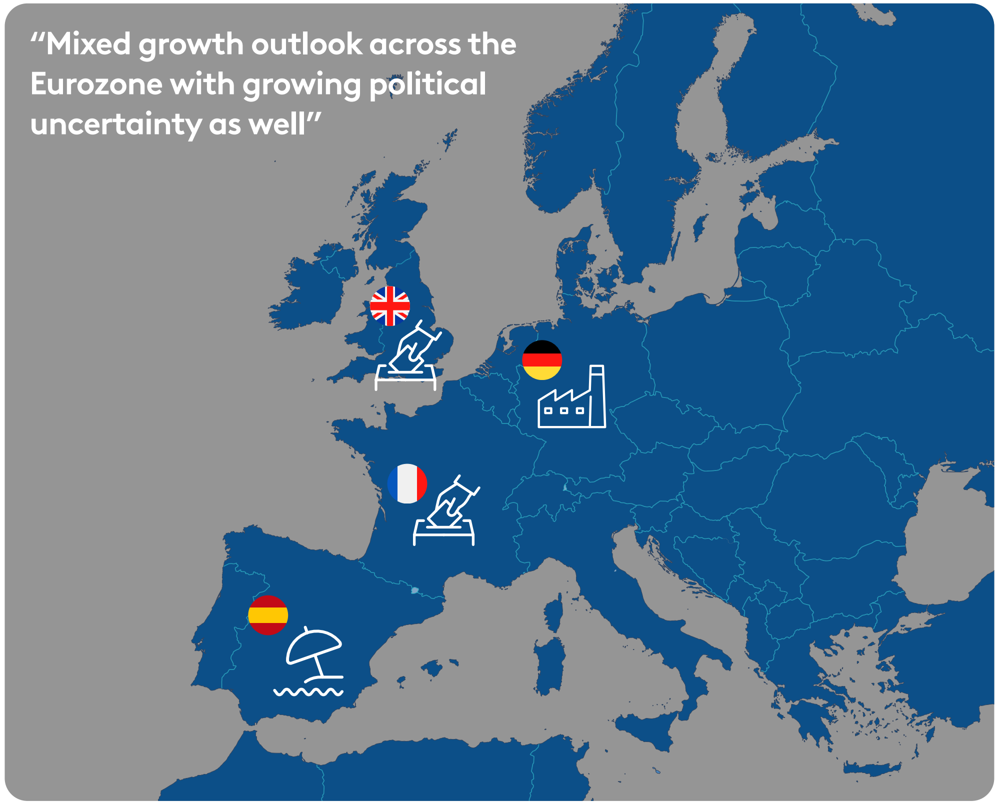


YTD shows year to 30 September 2024. QTD shows quarter to 20 September 2024. Indexes or prices used are: US equities - MSCI USA Index, European equities - MSCI EU Index, DM gov. debt - Bloomberg Global Treasury Index, Emerging debt - JPMorgan Emerging Market Bond Index (EMBI) Global Composite, High Yield - Bloomberg Global High Yield Index, IG credit - Bloomberg Global Credit - Corporate Index, US loans – Morningstar LSTA US Leveraged Loan Index, European Loans – Morningstar European Leveraged Loan Index, Cash - Bloomberg US Treasury Bellwethers: 3 Month Index.

While at the start of the year markets miscalculated the timing and speed of interest rate cuts, we are now seeing inflation trending towards central bank targets, which should lead to further rate cuts this year. The Federal Reserve ("Fed"), European Central Bank ("ECB") and Bank of England ("BoE") have all continued to signal an "easing off the brakes" approach to rate cutting, which suggests we will see a gradual movement towards neutrality. All three central banks have indicated rate cuts are likely to continue in Q4, though we wouldn't expect to see another 'jumbo' rate cut as we saw from the Fed in September. The easing of monetary conditions is expected to reinvigorate M&A and IPO activity after several muted years, creating new opportunities in the market. However, as recent developments have demonstrated, the situation remains fluid and susceptible to rapid changes.

The macro picture remains unclear as we enter Q4. The US economy has slowed over the last few months but remains in good shape overall. The increase we've seen in the unemployment rate was mainly a result of an increase in supply in combination with a lack of hiring, rather than mass redundancies. The 50bps Fed cut, and guidance towards further cuts, should give a boost to some of the sectors that were under most pressure from restrictive rates. The focus will increasingly shift towards 5th November as the US presidential election appears too close to call. The result will boil down to less than a handful of swing states. The divergence in candidate policies is perhaps one of the most stark in recent memory and as such the range of outcomes in relation to domestic and international policy means it is difficult to determine how the US will position itself in 2025 until the election concludes. We may see a pick-up in hiring after the elections as corporates are on the fence right now given the lack of clarity around tariffs, infrastructure spending and corporate taxes among other policy areas. One of the few things that many people seem to agree on is that both candidates' policies appear to be inflationary, even though the underlying drivers for this inflation are different. It's also unclear whether Fed Chairman Powell will still be in post after the election, which makes the outlook for rates even more difficult to call.

The situation in Europe is markedly different to the US, growth remains challenging and uneven across the Eurozone. PMIs continue to disappoint – the services sector is still holding up reasonably well in the post-COVID boom but manufacturing is struggling. Germany continues to be hampered by a number of structural issues, namely its ageing population, energy dependence and heavy reliance on the exports of goods to China. Fiscal policy has also not supported growth, as the government insists on keeping its budget deficit low, thereby hampering potential stimulus. By contrast, Spain benefits from a younger population, tailwinds from a booming tourism sector, considerable investment in infrastructure and cheaper gas imports from northern Africa. The difference in trajectories for Eurozone countries makes the ECB's job even more complicated. In addition, there remains significant political uncertainty in a number of countries.



In the UK, the landslide victory of the Labour government should result in greater stability after high turnover in Downing Street under the Conservatives in recent years. However, the honeymoon period already appears to be over and all eyes are fixed on the October budget which will be a critical juncture if Labour are to start to deliver on some of their election promises to kickstart the economy. Similar to the Fed and the ECB, the BoE started the cycle of rate cuts but with inflation still above the BoE's target, rate cuts will be slow and gradual as evidenced by the BoE's decision to keep rates unchanged at their September meeting.

Finally, the geopolitical landscape has deteriorated in recent months, as the conflicts in Ukraine and the Middle East continue. The invasion of Kursk and President Zelensky's subsequent demands to allow Ukraine to deploy long-range missiles into Russia marks a significant escalation in the conflict, making a truce appear increasingly unlikely. Similarly, in the Middle East, despite pressure from the US, no ceasefire agreement has been reached between Israel and Hamas, and tensions have further intensified with the eruption of conflict in the north involving Hezbollah and Iran. These conflicts could have material impacts on commodity prices, supply chains and consumer confidence.

In summary, the outlook for the US, Eurozone, and UK economies remains difficult to predict. So far, corporate earnings have held up better than anticipated, while most central banks globally have started their easing cycle. This has driven a large number of equity indices to all-time highs. While inflation has come off the highs and is now much closer to central banks targets, there are still a number of factors that could re-ignite inflationary pressures. With lower rates and stronger corporate earnings, we have seen an acceleration in M&A activity even though we remain well below historic averages. Buyout funds have considerable dry powder available and we are starting to see signs that the lower cost of funding is starting to result in higher leveraged buyout ("LBO") activity.

Liquid Credit Markets

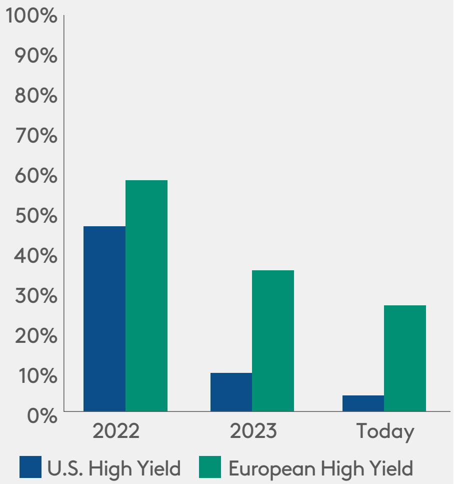
Despite bouts of volatility during the quarter, spreads have remained rangebound and close to historic tights, as risk sentiment remains solid, and investors continue to view leveraged finance as an attractive opportunity given the compelling all-in yields. High yield returns remain strong YTD at 7.7% in the US and 6.1% in Europe, while leveraged loans also continue to report strong performance, with US loans posting a 6.6% YTD return, and Europe 6.2%.[1]

Spreads in the US and Europe continue to grind tighter despite a turbulent macro environment. We have seen some bouts of volatility this year, for example around the French elections in June and fears of a US macro slowdown in August. However, these periods of volatility only lasted a few days as investors look at the all-in yield provided by loans and high yield bonds as an asset class and for now buy any dip they see in prices. The US high yield market is now trading within the 96th percentile of historic spread levels, but all-in yields closer to the median compared to historic levels over the last decade. CCCs continue to outperform as earnings are generally holding up well. Distress ratios – as an indicator of future default activity – continue to decline marginally, implying that fundamentals in the liquid sub-investment grade markets are in relatively good shape.

"Spreads whipsawed during the quarter but ultimately continue to grind tighter. All-in yields remain compelling for investors"

Exhibit 2

U.S. & European High Yield Spreads Percentiles Relative to Historical Levels

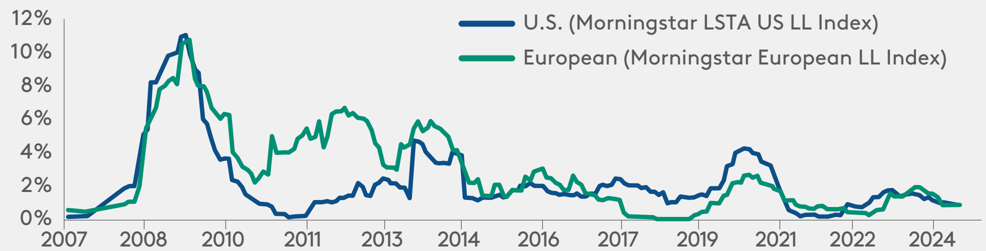


Data through 30 September 2024. Source: Credit Suisse. Percentiles ranked vs. monthly spread to worst data starting 01/31/2000. 2022 represents 30 December 2022, 2023 represents 29 December 2023 and 'Today' represents 30 September 2024.

Despite concerns of a macro slowdown, credit fundamentals appear resilient, with defaults remaining benign in both the high yield and leveraged loan markets. Similar to last quarter, US high yield default rates continue to tick downwards, now at 1.4% on a rolling twelve month par-weighted basis, although European high yield default rates have spiked recently at 2.8%. Leveraged loan defaults continue their downwards trend, with both Europe and the US reporting 0.8% default rates. It's worth noting that this default cycle has been less severe than previous default cycles, and materially below the levels what some people were forecasting when central banks started hiking base rates. Defaults appear to be largely concentrated on smaller firms, which are defaulting at 1.8x the rate of larger institutions (source: Deutsche Bank). When factoring distressed exchanges into default rates they are considerably higher, although these exchanges do not necessarily lead to a loss of capital, which is why they are excluded from our figures. Generally, we also find default rates to be higher for non-sponsored businesses compared to sponsored businesses, especially when taking distressed exchanges into account. Typically families will be more protective of the business they have built, and don't necessarily have a longer term reputation to protect like a sponsor.

Exhibit 3

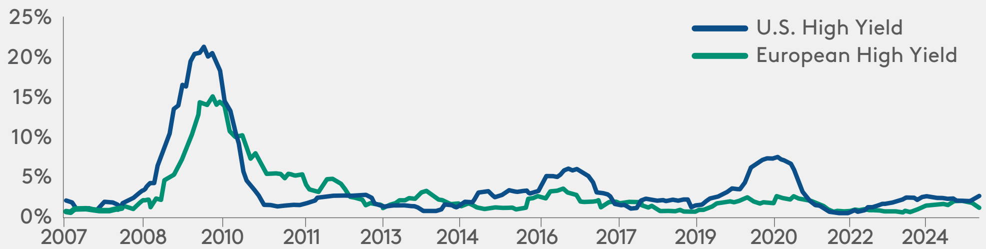
U.S. & European Leveraged Loan Last 12-Month Default Rate: Principal Amount



Data through 30 September 2024. Source: Pitchbook LCD; Morningstar LSTA US Leveraged Loan Index; Morningstar European Leveraged Loan Index.

Exhibit 4

U.S. & European High Yield Last 12-Month Par-Weighted Default Rate



Data through 30 September 2024. Source: Bank of America Global Research.

1 As of 30 September 2024. US High Yield represented by the Credit Suisse High Yield Index (USD Hedged). European High Yield represented by the Credit Suisse Western European High Yield index (EUR Hedged). US Leveraged Loans represented by the Credit Suisse Leveraged Loan Index (USD Hedged). European Leveraged Loans represented by the Credit Suisse Western European Leveraged Loan Index (EUR Hedged).

Downgrades continue to outpace upgrades, particularly in the European leveraged loan market, although this has not, as previously noted, led to a surge in defaults. This is in-line with our expectations that marginal credit deterioration was likely after a prolonged period of elevated rates and tight financial conditions. We continue to see rising stars outpace fallen angels in high yield ($31bn vs. $76.bn within US high yield), but within the capital structure downgrades have outpaced as credits contend with elevated rates and subdued growth.

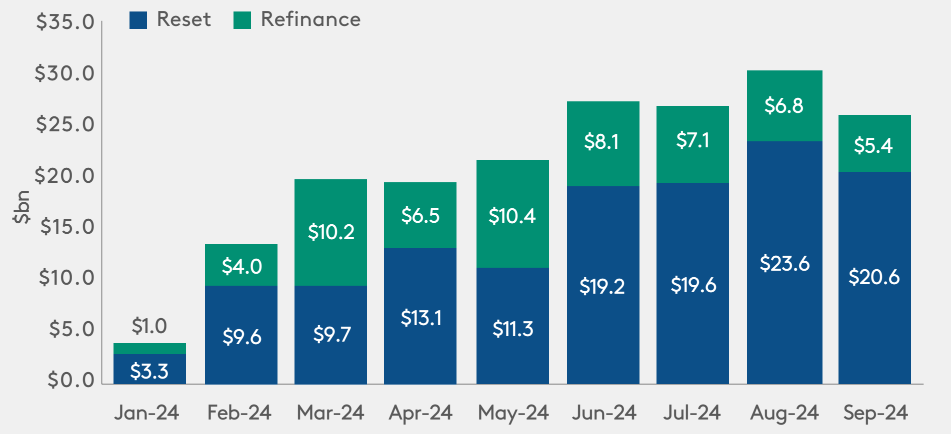
> **"The maturity wall for both high yield and leveraged loans is now well-positioned, with the majority of maturities now pushed out to 2028 and beyond"**

Issuance continues to be strong, though it was seasonally more muted during July and August, total issuance in the US leveraged loan market now exceeds $509bn year-to-date while European issuance is now in excess of €80bn. The high yield bond market has also experienced strong issuance, with c.$240bn of new issues in the US high yield market, already in excess of the total for 2023 ($175bn) as market access continues to improve. It's worth noting that the large majority of this supply has been refinancing related. In the US leveraged loan market alone, refinancing activity accounted for over $255bn of this year's supply. The maturity wall for both high yield and leveraged loans is now well-positioned, with the majority of maturities now pushed out to 2028 and beyond. M&A related volumes continue to lag when compared with historical issuance, although we would expect this to gradually increase as rates continue to be cut, which should improve confidence and spur greater activity in the market. CLO issuance also remains close to double the volume of 2023's issuance at this stage and there remains sustained levels of demand for new issues which has resulted in a technical supporting of spreads.

The supportive technical environment has been particularly beneficial for CLO managers, with S&P Global Ratings estimating that US CLO managers could achieve record refinancing and reset volumes by the end of the year. This has also been true within CVC's CLO business, which has executed six US refinancings and resets, as well as three further European refinancings / resets during the year. In Europe, CVC recently priced the second reset of Cordatus VI, a €400m European CLO the firm have been managing since March 2016, extending the Reinvestment Period by c.4.5 years. This transaction means the CLO is on track achieve a c.14% net Equity IRR, and 2x+ MOIC, having already achieved a ~1.3x MOIC. In the US, CVC recently priced the reset of Apidos CLO XLI, which will extend the Reinvestment Period by 5 years. The transaction was very well received by the market and the CLO priced at the tight end of the market with a weighted average running cost of debt of 3mS + ~173bps, representing debt cost savings of over ~103bps. CLO equity investors in general have been significant beneficiaries of the favourable market environment, with Deutsche Bank estimating that if the pace of distributions remains on track for the rest of the year annual returns could be in excess of 19% which would be the highest equity distributions recorded during the European 2.0 CLO period. Similarly, CVC's own CLO equity vehicles continue to perform strongly. Notably, CLO Equity I (2017) is now recording an underlying CLO annual yield of 18.2% and 1.7x MoM, whilst CLO Equity II (2021) enjoys a 20.7% underlying CLO annual yield and 1.5x / 1.4x gross / net MoM.[2]

In terms of positioning, we started the year by reducing our fixed rate high yield exposure in our flagship Global Yield fund due to the market pricing in too many rate cuts given where inflation and the economy were trending. This was the correct decision and the carry from floating rate loans outperformed the convexity offered by fixed rate high yields. During the summer, we added high yield exposure to the portfolio as inflation has begun to moderate and central banks have started their rate cutting cycles across the globe. We are likely to continue to add fixed rate exposure, in particular in Europe where softer macro data may increase the pace of rate cuts by the ECB. Given how tight spreads are in the US, and

Exhibits 5
US & European CLO Reset and Refinancing Volumes



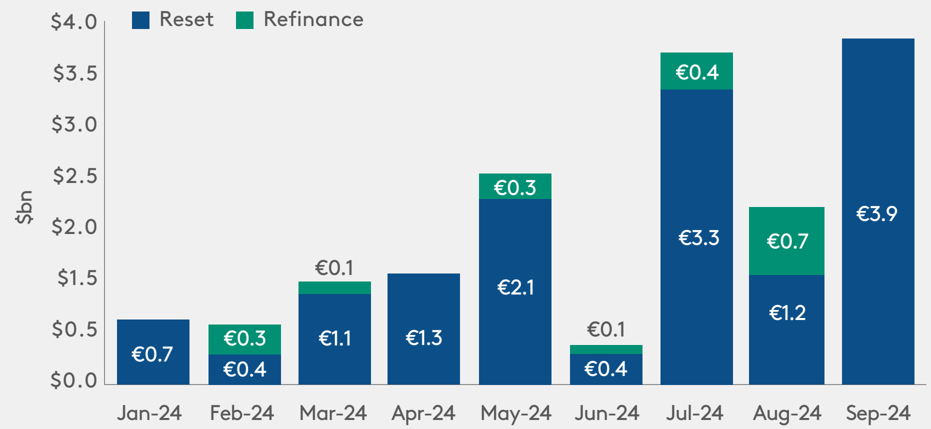
Source: J.P. Morgan CLO Weekly Datasheet, data excludes Private Credit / Middle Market deals. Data as at 30 September 2024.

2 Please note, the Underlying CLOs Annual Yield incorporates the distribution yield of the underlying CLOs, rather than the Fund structure. The Underlying CLOs Annual Yield is net of fees at the CLO level. The SEC net return (based on the application of a model fee that reflects the effective of fees at the fund level), is 15.8% (CLO Equity I), 18.0% (CLO Equity II) and 15.0% (CLO Equity III). Performance has been calculated using the ratio method of gross/net for CVC Credit CLO Equity III fees and expenses and is 0.87x, based on 17.0% gross and 14.8% net. Gross and net IRR and MoM reflect actual returns rather than the application of a model fee. Net MoM calculated as net asset value plus all distributions (income and capital), divided by total draws. Gross MoM adds back historical expenses.

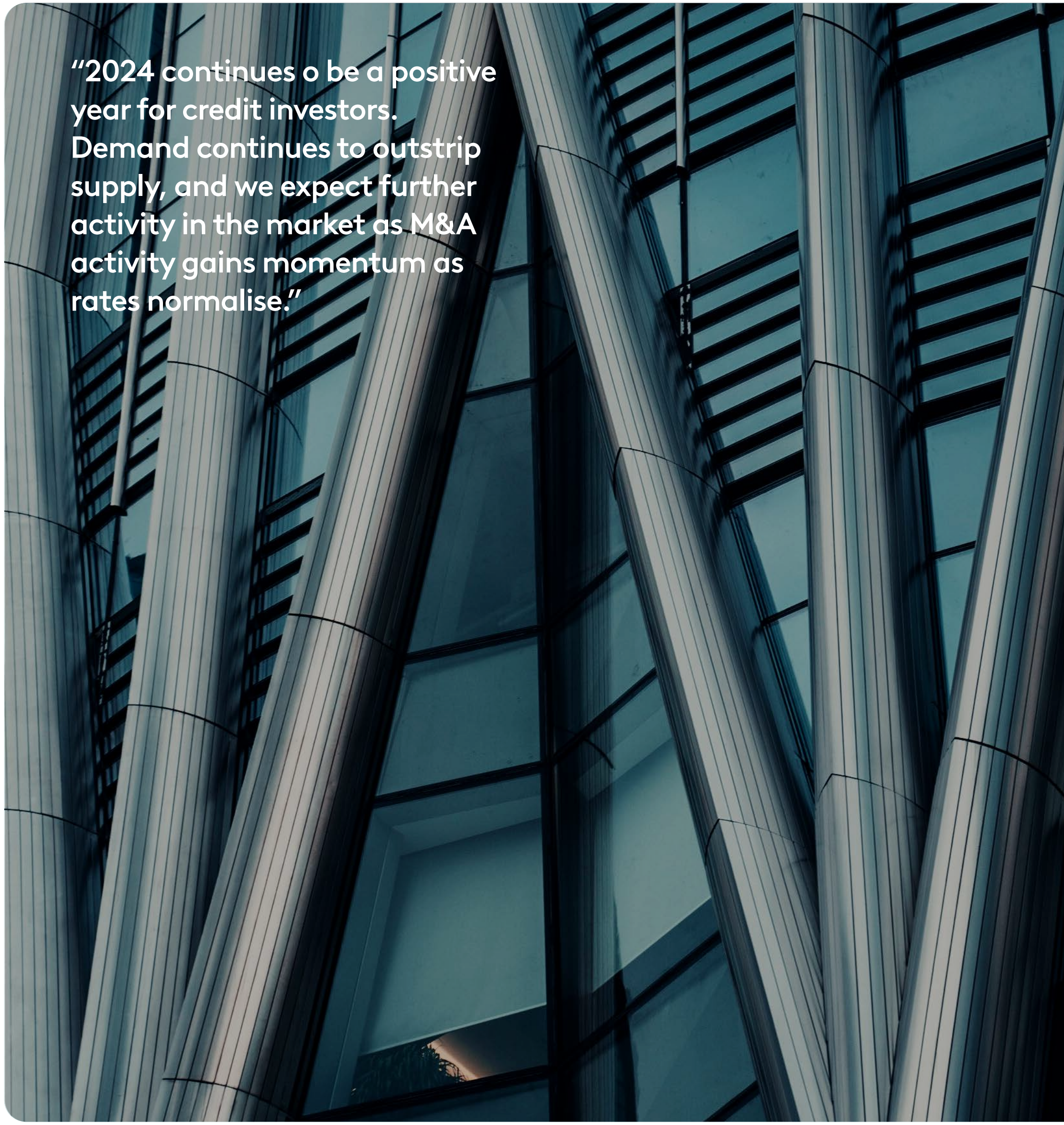
the better macro outlook, we feel it's unlikely the Fed will do another outsized 50bps cut in its November meeting, but is more likely to revert to a number of 25bps cuts over the next few meetings. We have rotated portfolios more towards Europe to pick up additional spread but continue to monitor deteriorating macro data in Europe. We will re-asses this position as we gain more clarity on Q3 earnings in October and November.

2024 continues to be a positive year for liquid credit investors despite valuations being rich given the high all-in yield investors are still able to capture. Demand continues to outstrip supply, supporting spreads from a technical viewpoint, and we expect further activity in the market towards the backend of the year as M&A activity gains momentum as rates normalise. As expected, there has been some marginal credit deterioration in both the high yield and leveraged loan markets as the higher cost of financing is having an impact on free cash flow generation. Downgrades outpaced upgrades, yet defaults have remained close to historic averages, as we anticipated. Nonetheless, the importance of active management remains clear, particularly as dispersion increases and markets remain volatile.

Exhibits 6
US & European CLO Reset and Refinancing Volumes



Source: J.P. Morgan CLO Weekly Datasheet, data excludes Private Credit / Middle Market deals. Data as at 30 September 2024.



Private Credit Markets

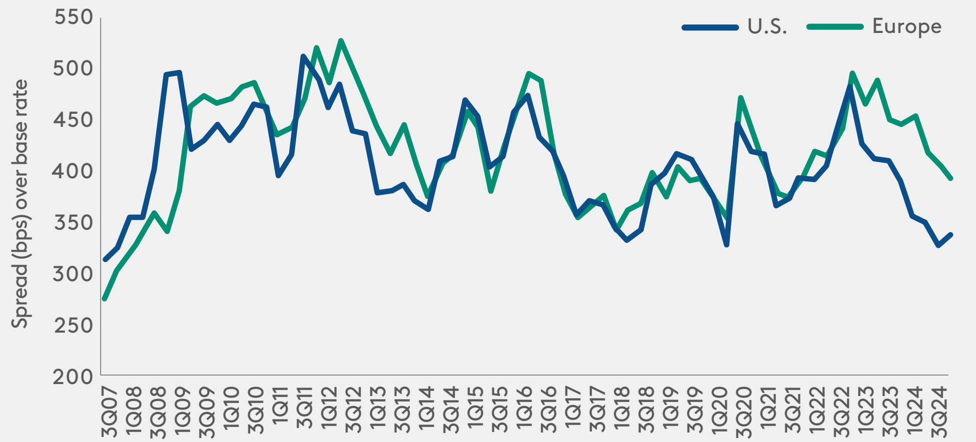
The themes of record high refinancing issuance in the broadly syndicated loan market have been felt within private credit, as spreads have compressed due to competitive refinancing processes. Nonetheless, there remains a clear opportunity in the middle and upper middle-market space, with names operating in this segment of the market unable to access the liquid credit markets as easily as larger issuers, presenting a clear opportunity for direct lenders such as CVC. Moreover, we continue to see strong inflows into the asset class from both institutional and retail investors, as private credit establishes itself as a key asset in a diversified portfolio.

Last quarter we noted that there were clear signs of spread compression in the private credit market as a result of the reopening of the broadly syndicated loan market, and there was a rebalancing within leveraged finance after a lack of public issuance throughout 2023. Lincoln estimate spreads have compressed by on average c.50bps in Europe and the US since the turn of the year,[3] although Configure Partners have noted that in recent months the pace at which private credit loans were being taken out by the broadly syndicated market has slowed as the balance between public and private markets recalibrates.[4] Deal flow within the middle and upper-middle market remains strong, as these issuers cannot easily access the public markets. Indicative of this, over the last quarter CVC's Private Credit team have signed a further eight direct lending transactions as sponsors continue to seek flexible alternative financing to support their transactions. These transactions remain consistent with our investment philosophy, partnering with leading sponsors, leveraging the CVC Network to support extensive due diligence, and supporting leading businesses in their markets. We expect deal flow to remain strong through to the end of the year as M&A markets pick up further, and private equity investors look to deploy their ever-growing arsenal of dry powder.

"BSL revival sparks competition, but middle-market lenders hold their ground"

As competition increases between not only private credit lenders, but also the broadly syndicated market, the ability to source a wide scope of transactions remains critical when selecting a private credit manager. CVC Credit continues to benefit from the wider CVC Network, leveraging the experience and expertise of over 270 private equity professionals and gaining direct access to its established network of 12 European offices to support the sourcing and due diligence process for transactions. This has resulted in the network supporting the Private Credit team across 71 transactions since 2021 and deploying €8.2bn in capital, representing 21 teams across the firm, exemplifying the integration between the Private Equity and Private Credit teams. However, the themes of origination remain broad among transactions. Whilst

Exhibit 7
Average New-Issue Institutional Spreads: Europe & U.S.



Source: Pitchbook | LCD. Data tthrough 30 September 2024.

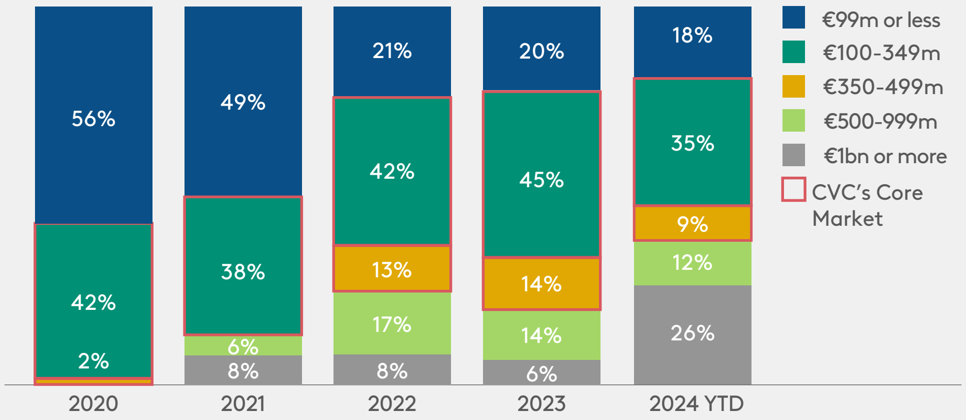
refinancings have remained a key theme, such as our recent refinancing and add on for Soderberg & Partners, a leading Nordic insurance broker backed by KKR and TA Associates, we have also seen new opportunities come to market from sources such as secondary LBOs and public to privates, as buyout activity continues to ramp up as expected. Transactions such as our financing in support of the acquisition of Superstruct Entertainment by KKR, and the public to private acquisition of Alpha Financial Market Consulting are recent examples of this resumption in activity. As M&A volumes continue to rise, and CVC's Private Equity platform continues to review an increasing number of transactions, this trend will likely only increase.

There have been concerns regarding operating metrics for select names within the market, but in general credits continue to report robust performance despite the mixed macro-outlook. For instance, Lincoln noted that 79% of European private companies covered in their universe reported YoY LTM revenue growth, whilst 69% reported YoY LTM EBITDA growth, which has increased

"Leveraging Scale: CVC's network drives sourcing and diligence in a competitive market"

3 Source: Lincoln International Partners. As of July 2024.
4 Source: Pitchbook. As of September 2024.

Exhibit 8
Deal size diversification of European direct lending deals, by count



Source: Pitchbook | LCD. Data through 30 September 2024. Analysis based on transactions covered by LCD News; share calculated based on deals where size information is disclosed.

for the last three quarters. Although the rate of revenue growth has slowed since last year, it remains positive across all sectors, with Healthcare and Business Services being the strongest performers in terms of sector performance, industries which CVC favours due to their defensive nature and cash generative features.

EBITDA margins also remain stable, with Consumer in particular showing strong signs of growth after previously struggling with high inflation which is now normalising.[5] As a result, we continue to see generally solid performance among European private assets, and whilst the rate of growth may have slowed versus prior years borrowers are still growing and reporting robust operating metrics.

Furthermore, managers continue to adopt a conservative approach to underwriting, with an increasing emphasis on documentation another notable trend during the quarter. As the macro environment begins to slow borrowers are increasingly emphasising provisions in documentation to tighten terms and ensure high underwriting standards. Morningstar DBRS noted that there has been a clear deviation between the quality of issuers, with some service providers issuers particularly vulnerable to interest coverage deterioration due to margin compression from persistent cost inflation, which they have struggled to pass through to customers. As a result, CVC continues to maintain a conservative approach to deployment, targeting defensive, market leading businesses, and with transactions over the last twelve months having an average LTV of c.35%. The importance of prudent credit selection and regular monitoring remains clear.

Finally, investor appetite for private credit remains sustained, despite the reopening of the broadly syndicated loan markets, with strong inflows into the asset class from both institutional and retail investors. At the midpoint of 2024 Pitchbook estimated c.$91bn had been raised in private debt through 59 different funds. This figure is a similar pace to the capital raised in 2023, although the number of funds raising has decreased significantly, suggesting there is an element of consolidation at play in the market as investors rally behind experienced GPs with long-term track records to navigate the increasingly complex macro environment. Notably, 96% of capital raised to date has been for 'experienced managers', the highest proportion on record.[6] By contrast, in 2023 this figure was 91%, and as recently as 2021 over 40% of funds in the market were emerging firms. Similarly, retail demand for private credit continues to grow, with CVC-CRED, our open-ended private credit product, receiving strong inflows since launching earlier this year. Performance has been above expectations in recent months and the fund is an exciting proposition for both institutional and retail investors looking to deploy into a ramped and well-diversified portfolio of assets with quarterly distributions and liquidity.

The private credit market is currently shaped by several intersecting forces, with refinancing activity remaining at the forefront, amid compressed spreads driven by a resurgent broadly syndicated loan (BSL) market. Despite this, middle-market opportunities remain compelling, particularly for direct lenders with a deep understanding of the middle market. Amid heightened competition between private credit and the broadly syndicated market, CVC continues to leverage its expansive network to enhance transaction sourcing and due diligence, a pivotal advantage versus competitors. Moreover, the importance of GP experience, long-term track records and consistent portfolio monitoring has come into sharper focus amid growing credit deterioration, with bifurcation now evident.

Investor demand for private credit remains robust, despite the resurgence of syndicated markets. Institutional and retail inflows continue apace, with a discernible shift toward experienced managers, signalling a consolidation of capital within the sector. This reflects confidence in established players' ability to navigate a complex macroeconomic backdrop.

As market dynamics evolve, private credit remains a critical component of diversified portfolios, with its unique ability to balance risk and opportunity in an increasingly competitive and uncertain environment.

"Conservative underwriting and strong documentation are becoming increasingly important in a turbulent macro environment"

5 Source: Lincoln International Partners. As of July 2024.
6 Source: Pitchbook. As of 30 June 2024.

Important Information:
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