

Pearl Diver Credit Company (NYSE: PDCC)

Rating: Buy

Price Target: \$20.00

Share Price: \$17.48

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Signs of stability in uncertain markets

Reiterate BUY Rating and \$20.00 Price Target.

Summary

Pearl Diver Credit Company Inc. ("PDCC"), an externally managed closed-end investment company that invests primarily in collateralized loan obligation (CLO) tranches reported a NAV of \$18.48, as of July 31, 2025. PDCC's strategy is to generate high recurring current income by acquiring *junior* CLO securities (equity and sub-debt tranches) secured by pools of floating-rate senior secured corporate loans by mainly U.S. issuers. Per the recent reporting quarter, the portfolio is diversified across 1,800 underlying loans with 1,285 unique underlying obligors and industries with 100% USD exposure. The top three industry exposures include Software (8.1%), Healthcare (4.7%), and Hotels, Restaurants, and Leisure (4.6%), showing an increase in the hospitality sector in comparison to prior quarters. The underlying loans are typically non-investment-grade (predominantly BB/B-rated) secured loans. The NAV of the PDCC portfolio was \$125.6 million as of July 31, 2025, at approximately \$18.48 per share. The NAV improved by \$0.15 from the prior quarter due to a combination of spreads compression in overall credit markets and realized gains of approximately \$0.5M. The Company also reported recurring cash flows from CLO investments of \$8.0 million, or \$1.18 per share for the quarter, above the payout ratio of distributions.

After the volatility in credit markets post Liberation Day (April 2, 2025), which caused several U.S. trading partners—including China, Canada, and the EU—to adopt retaliatory and countermeasures, credit spreads have stabilized this quarter.

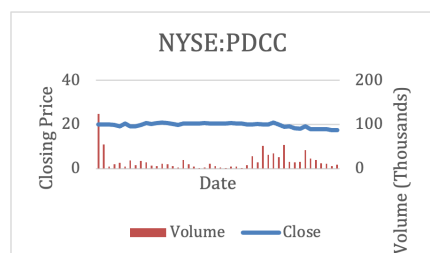
Company Data

Average Daily Volume (M)	0.0039
52-Week Range	17.37-21.90
Shares Outstanding (M)	6.796
Market Cap (M)	117.20
Enterprise Value (M)	144.40
Total Cash (M), mrq	0.18
Total Debt to Assets	24.2%

Estimates

FYE: Dec		2024A	2025E
NAV	Q1	N/A	\$18.33
	Q2	N/A	\$18.48
	Q3	\$20.05	
	Q4	\$19.89	
EPS	Q1	N/A	-\$0.90
	Q2	N/A	\$0.46
	Q3	\$0.48	
	Q4	\$0.51	
NII/Share	Q1	N/A	0.503 A
	Q2	N/A	0.52 A
	Q3	\$0.401	0.52 E
	Q4	\$0.504	0.52 E

One-Year Performance Chart



As of September 3, 2025. Source: MarketWatch

We estimate PDCC will continue to pay **\$0.22/ share** in monthly dividends in the medium-term range, representing a current yield of approximately **15%**. Our estimate is based on current CLO yields, the credit outlook for U.S. credits, and management's strategy of active credit and loss management, generating **total returns** in the mid-teens range.

PDCC's stock is trading around \$17.50, and we are re-iterating our \$20 price target and a **Buy** rating. We are basing our target price at 1.08x NAV.

As indicated in our initiation report of June 30, 2025, we expect the portfolio NAV to stabilize after declining in Q1 2025 and to also show improvement from current levels, based on current market conditions and the near-term outlook on U.S. credits. Our evaluation is also based on our confidence in management's capability to manage near-term risks and a strong and rigorous quantitative approach in credit selection, evaluating mispriced credits in the secondary markets and underwriting new loan issuance.

Q2 2025 Overview

PDCC's portfolio NAV is highly correlated with prevailing sentiment in credit markets and fluctuates with movement in credit spreads, particularly in the non-investment-grade space. The share price has historically tracked movements in NAV, and we expect this to be a key feature in evaluating the investment opportunity in PDCC. Net income improved to \$0.52/share in Q2 2025, from a loss of (\$0.90)/share in Q1 2025. This was largely driven by mark-to-market movements and realized gains of \$0.5M, resulting in Q2 2025 net investment income (NII) of \$0.46/share, compared to (\$1.41)/share in the prior quarter. In our view, PDCC management has demonstrated expertise and discipline in managing credit origination and selection, leading to below-benchmark loss rates of approximately 0.7% in their overall portfolios. This trend continued in Q2 2025, with the PDCC approach of underwriting new issues and evaluating mispriced credits in the secondary markets consistent with their traditional quantitative approach. The positive carry on the portfolio's Weighted Average Spread (WAS) and weighted average cost of capital (WACC) remained strong on a total return basis, allowing management to keep distributions consistent without impacting NAV. This was achieved despite a compression in yields, with weighted average portfolio yield of 12.57% during Q2 2025, compared to 15.57% in the prior quarter. Recurring cash flows from CLO investments remained strong at \$8.0M for the quarter (\$1.18/share) keeping it at levels in excess of its monthly distributions. We expect the NII/share to remain **stable at around \$0.50/share per quarter**, keeping yield in the **12-15%** range.

Strengths	Challenges
<ul style="list-style-type: none"> NAV continues to grow with spread compression and the U.S. Federal Reserve's interest rate outlook pointing to rate cuts later in 2025, providing strong returns on a total-return basis Strong manager track record with loss rates well below industry and benchmark indices over a 10-year period A sophisticated and quantitative approach to credit selection and active credit management using proprietary AI/ML algorithms Strong credit outlook for U.S. issuers and continued outperformance of the senior secured leveraged loan indices over Business Development Companies (BDCs) 	<ul style="list-style-type: none"> Inflationary pressures for U.S. credits remain due to potential increase in input costs caused by tariff uncertainties Underlying portfolio is a leveraged play on non-investment-grade credits that are most sensitive to market swings, potentially grinding the NAV Compression in credit spreads may result in a repricing of loans, resulting in mark-to-market losses

Portfolio Update Q2 2025

PDCC invests **through special purpose vehicles (SPVs)**. Each CLO is a bankruptcy remote special purpose vehicle that issues multiple debt tranches (rated AAA to BB) and retains an equity tranche. PDCC holds a mix of CLO equity and high yield CLO debt. PDCC has raised capital via common equity (shares) and 8% Series-A term preferred equity. PDCC's assets are predominately **CLO securities comprised of CLO equity tranches**. Each CLO SPV holds a pool of senior secured loans to corporate obligors (e.g. Asurion LLC, TransDigm Inc., Cloud Software Group). PDCC's top ten obligors each account for approximately 0.4–0.7% of NAV. The CLO's liabilities are issued to outside investors, and PDCC as an equity holder receives the residual cash flows after paying the CLO debt coupons.

PDCC's portfolio is highly diversified by issuer and sector. As noted, it held approximately 52 different CLO equity investments across 31 CLO managers as of Q2 2025, with exposure to 1,285 unique corporate obligors and 1,800 underlying loans. Each CLO is backed by a portfolio of senior secured loans to U.S. companies, spanning sectors such as technology, healthcare, consumer products, industrials, and energy. PDCC continues to **invest in equity and junior debt tranches of CLOs collateralized by portfolios of sub-investment grade, senior secured floating-rate debt, issued by many distinct U.S. companies across several industry sectors**. The portfolio's underlying loan base has an **average credit rating in the B+/B range**, reflecting broad exposure within the high-yield loan market. Weighted average portfolio yield was 12.57 % in Q2 2025, due to market-wide loan spread compression.

Leverage has been limited (roughly 24.2% of assets in debt as of Q2 2025), via margin and a preferred stock offering, and liquidity of the CLO equity positions is strong through broker markets.

Credit Quality: Q2 2025

PDCC's assets are mainly non-investment-grade, and CLO equity is unrated. Underlying loans in the PDCC portfolio for the quarter included many highly leveraged borrowers (e.g. tech and healthcare leveraged buyouts), with a slight increase in exposure to the hotels, leisure and hospitality sectors, that experienced active refinancing activity. There was no other notable change in the credit quality of the portfolio in the last quarter, with the focus remaining on non-investment-grade credits and 95% of the portfolio having re-investment end dates from 2026 through 2030. PDCC's effective portfolio yield of 12.17% reflects this risk profile. As of July 31, 2025, the aggregate fair value of investments of \$165.8 million far exceeded total debt of \$34 million, with an asset coverage of 398% per \$1,000 per preferred share.

Risks

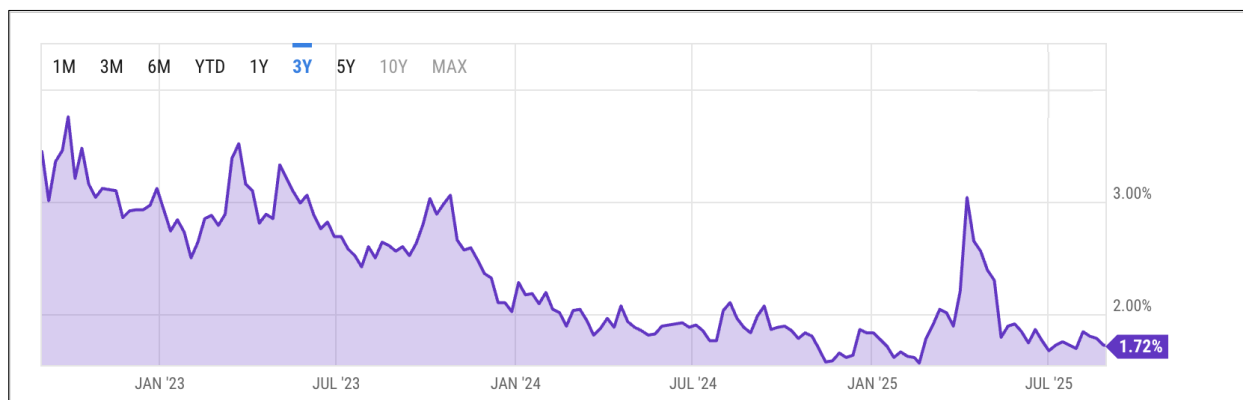
A key risk to the NAV of the PDCC portfolio is its sensitivity to interest rates. Rising interest rates are generally neutral to positive for PDCC, since most underlying loans are floating rate securities, with higher rates boosting loan coupons. Conversely, falling rates would reduce cash flows on floating loans. Tariffs or macro shocks that negatively affect corporate earnings could increase defaults: a 1-3% increase in loan defaults from the current very low levels could impair CLO equity values. However, PDCC's diversification mitigates default rate risk, accommodating up to a maximum of 3% of loans defaulting, based on stress tests on the underlying portfolios. This also accounts for net loss rates (actual defaults) for senior secured loans in the 30-35% range with recovery rates at 65-70%. These default rates would modestly impact equity tranches given over-collateralization and multi-year amortization. In stress scenarios, PDCC's NAV would drop as CLO valuations fall, but the high-yield (15%+) coupon stream and credit hedges (e.g. diverse industries) would mitigate some of the impact. A key feature of PDCC's portfolio performance has been the historic loss rate since inception of their funds. PDCC has tracked loss rates in its senior secured loan book of approximately 0.7%, well below the loss rates tracked by benchmark indices. The fund's value will fluctuate with loan spreads and the prevailing macro-environment in credit markets. In the past quarter PDCC showed unrealized mark-to-market gains of \$0.5M that was preceded by a loss of \$9.6M in Q1 2025. Inflationary pressure bringing about higher interest rates is a potential headwind that could result in higher credit spreads for non-investment grade credits. This was evident in 2022 when the Federal Reserve went through a tightening period with a 500bp rate hike to offset inflationary pressures, but PDCC's robust credit selection process coupled with a strong performance in the senior-secured loan space proved to be mitigating factors.

Fees and Expenses Q2 2025

PDCC's advisory fee is **1.50% p.a. of total equity** (calculated quarterly). There is also an **incentive (performance) fee** of 15% of net investment income above an 8% annualized hurdle return with a built-in "catch-up" feature of 2.35924% per quarter (9.42% annualized). No fee is paid unless quarterly NII exceeds 2.00% per quarter (8% annualized hurdle rate). The incentive fee paid out for Q2 2025 was \$547k, slightly less than the incentive fee of \$604k in the prior quarter, despite realized gains of \$0.5M

in the quarter. The fund's reported expense ratio (annualized since inception, per last filings) is approximately 6.60% including all operating expenses, interest expense, and incentive fees, and about 3.50% excluding interest expense and incentive fees.

U.S. Credit Markets & Leveraged Loans

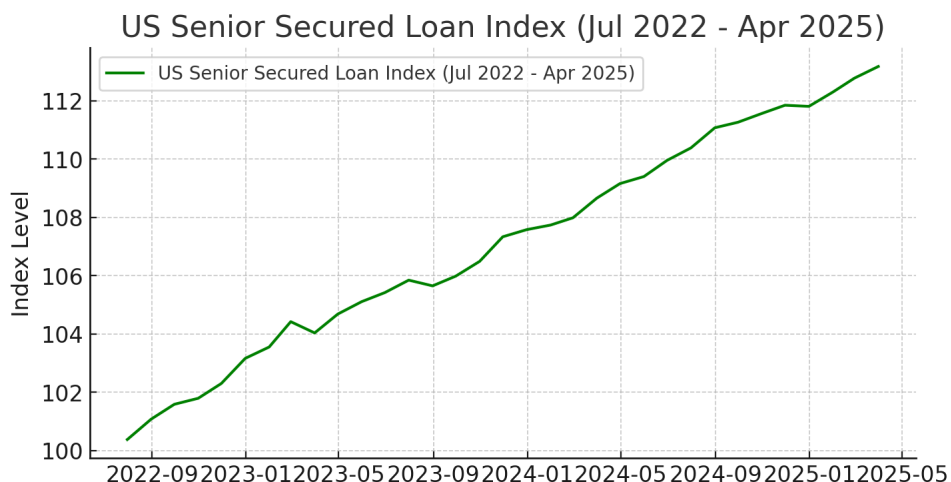


Source: FDIC: OAS spreads, BB high yield index

Senior Secured Loans

As of Q2 2025, BB-rated high yield spreads compressed significantly after the spike, post Liberation Day announcement. This reflected an increased investor appetite for spread product, with effective yields tracking lower as Treasury yields increased but risk premiums narrowed. The U.S. leveraged loan market (e.g. the LSTA senior secured loan index) continued to deliver positive returns carrying yields higher than BB bonds (often in the 7.0–8.0% range). High yield and loan spreads remained tight by historic standards, but widened briefly on macro news, post the Liberation Day announcement. As of Q2 2025, HY bond spreads fell in the 270 bp range, while leveraged loan discount margins remained above historical medians in the 470 bp range. U.S. banks increased provisions relative to pre-2022 averages, reflecting heightened default activity, particularly in riskier sectors, but outlook for U.S. credits remains benign. The S&P Leveraged Loan default rate remained in the 3.0-3.5% range, versus the HY bond default rate range of 1.0-1.5%. PDCC portfolios continue to track default rates below the broad indices by adopting a rigorous quantitative approach. This has been explained in detail in our initiation report dated June 30, 2025.

The loan market has seen **16 consecutive months of positive total returns** through mid-2024, driven primarily by carry in a high-rate environment. This bodes well for PDCC's CLO portfolios whose performance is highly dependent on their loan origination capabilities and exploitation of arbitrage opportunities.



Source: FDIC

Valuation and Outlook

PDCC is a permanent capital vehicle paying monthly dividends of \$0.22/share. We expect dividends to be stable in the medium-term and NII/share to remain in the \$0.50/share-\$0.55/share range per quarter. We expect the NAV to continue to remain stable and grow moderately in the near term. Notwithstanding the tariff shocks, we expect a benign credit environment for senior secured loans and falling credit spreads for non-investment grade debt. We issue a **BUY** rating on the stock on this basis, with a price target of approximately 1.09x NAV, or \$20 per share. This is consistent with our initial rating on the stock in June 2025.

Financials

Pearl Diver Credit Company										
Earnings Model										
Year	2024		2025				2026			
Quarter	Q3	Q4	Q1	Q2	Q3E	Q4E	Q1E	Q2E	Q3E	Q4E
Total Assets	137,587,304	179,071,696	173,655,377	166,128,736	166,533,701	167,083,701	167,613,701	168,153,701	168,709,701	169,284,701
Total Liabilities	1,316,841	14,865,808	15,680,829	9,069,614	9,069,614	9,069,614	9,069,614	9,069,614	9,069,614	9,069,614
Preferred Shares	0	28,990,243	33,393,885	33,445,477	33,445,477	33,445,477	33,445,477	33,445,477	33,445,477	33,445,477
Net assets	136,270,463	135,215,645	124,580,663	123,613,645	124,018,610	124,568,610	125,098,610	125,638,610	126,194,610	126,769,610
Total Investment Income	3,946,115	5,439,244	6,015,004	5,508,431	6,063,220	6,087,473	6,111,823	6,136,270	6,160,815	6,185,459
Yields										
Calculated Annual Investment Yield on Average Total Investments	11.77	13.91	14.84	12.58	13.98	14.04	14.10	14.15	14.21	14.27
post-Incentive Fee Annual Yield	7.998	10.137	10.981	9.965	11.455	11.509	11.564	11.619	11.674	11.729
Expenses:										
Incentive fee	480,420	604,720	603,528	547,708	589,529	591,476	593,353	595,264	597,232	599,268
Professional fees	63,486	45,544	7,815	0	7,815	7,815	7,815	7,815	7,815	7,815
Total Fees	1,187,557	1,947,025	1,679,198	1,573,619	1,629,417	1,636,676	1,643,863	1,651,189	1,658,698	1,666,413
Interest Expense:	0	54,168	854,888	831,122	854,888	854,888	854,888	854,888	854,888	854,888
Offering costs	0	11,294	60,914	0	11,294	11,294	11,294	11,294	11,294	11,294
Total expenses	1,221,240	2,012,487	2,595,000	2,404,741	2,495,599	2,502,858	2,510,045	2,517,371	2,524,880	2,532,595
Net Investment Income	2,724,875	3,426,757	3,420,004	3,103,690	3,567,621	3,584,615	3,601,778	3,618,899	3,635,935	3,652,864
Net investment income per share	0.401	0.504	0.503	0.457	0.525	0.527	0.530	0.532	0.535	0.537
Net income per share	0.480	0.505	-0.904	0.537	0.525	0.527	0.530	0.532	0.535	0.537

DISCLOSURES

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Distribution of Ratings				
Kingswood Capital Partners, LLC				
Investment Banking Services/Past 12 Months				
Rating	Count	Percent	Count	Percent
BUY	10	83.33	2	22.22
HOLD	1	8.33	0	0.00
SELL	0	0.00	0	0.00
NOT RATED	1	8.33	1	100.00

As of August 2025

Kingswood Capital Partners received compensation from Pearl Diver Credit Company during the past 12 months. Kingswood is not currently engaged by Pearl Diver Credit Company to provide investment banking or advisory services.

Pearl Diver Credit Company Rating History as of September 4, 2025



Source: E-Trade.

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