

Thirdpath

*Middle-Market
Direct Lending:*

A Comparison of
Investor Access Points

Key Takeaways

- 1 Access structure materially affects risk and convexity**
Public BDCs, private BDCs/interval funds, institutional funds, and secondary purchases each offer different combinations of liquidity, transparency, fee drag, downside protection, and return potential.
- 2 Discounts to NAV embed convexity**
Public BDCs currently trading at ~20% average discounts (with some 25–30%) introduce both yield enhancement and potential re-rating upside, similar to secondary fund purchases acquired below NAV.
- 3 Secondary purchases and public BDC discounts are thematically aligned**
Both structures allow investors to acquire exposure at a margin of safety, mitigating J-curve effects and embedding downside protection.
- 4 Structure should reflect portfolio objectives**
Liquidity needs, scale requirements, fee sensitivity, and desired convexity will determine which access point is most appropriate within a broader private credit allocation.

Executive Summary

Investors seeking exposure to middle-market direct lending have multiple access points, each offering a distinct mix of liquidity, transparency, fees, convexity, downside protection, and return potential. We examine four primary routes—publicly traded BDCs, private BDCs/interval funds, institutional commingled funds and SMAs, and secondary fund purchases—and compare their structural characteristics to inform portfolio construction decisions.

Given current market conditions, particular attention is warranted around publicly traded BDCs, which are trading at average discounts of approximately 20% to NAV, with certain names at 25–30% discounts. These dynamics share thematic similarities with secondary fund purchases, where exposure is acquired below NAV, embedding convexity and a margin of safety compared to private BDCs and interval funds.

Publicly Traded BDCs

Examples of Certain Offerings: Ares Capital (ARCC), Oaktree Specialty Lending (OCSL), Golub Capital BDC (GBDC)

Liquidity: Daily trading on public exchanges.

Valuation: Market-driven; may trade at a premium or discount to NAV. Currently, the average public BDC trades at approximately a 20% discount to NAV, approaching levels seen during the height of the COVID-19 dislocation, with certain outliers (e.g., FS KKR Capital Corp. ~52% discount).

Access: Broadly accessible through brokerage accounts.

Fees: External management fees (generally 1–1.5% base + 15–20% incentive), in addition to public market trading dynamics.

Transparency: High—SEC filings, quarterly reporting, and daily market pricing.

Convexity: Typically limited under normal conditions, as returns are largely driven by coupon income. However, discounts to NAV typically introduce embedded convexity: investors may benefit from both dividend yield and price appreciation if discounts narrow.

Downside Protection: Enhanced when purchased below NAV. Discounts provide a margin of safety, cushioning potential NAV deterioration and improving yield-on-cost. This is particularly notable when BDC portfolios overlap with the manager's institutional direct lending strategies.

Pros: Immediate liquidity, accessibility, potential to acquire exposure at a discount.

Cons: Public market volatility can distort valuations relative to NAV; persistent discounts may impair a BDC's cost of capital.

Private BDCs / Interval / Evergreen Funds

Examples of Certain Offerings: Blackstone Private Credit Fund (BCRED), Owl Rock Technology Income Fund, Cliffwater Corporate Lending Fund (CCLFX).

Liquidity: Limited—quarterly redemption programs, often capped at approximately 5% of NAV per quarter.

Valuation: NAV-based, typically using third-party valuation agents.

Access: Targeted toward high-net-worth investors and wealth platforms; minimums generally \$25K–\$50K.

Fees: Comparable to institutional funds (often 1%+ management and 10–15% incentive), sometimes including additional distribution fees.

Transparency: Moderate—quarterly reporting without daily market pricing.

Convexity: Low to moderate; return profile is primarily income-driven, with relatively stable NAV marks.

Downside Protection: Greater apparent stability than public BDCs due to NAV smoothing and limited mark-to-market volatility. However, redemption gates may restrict liquidity during stressed markets

Pros: Lower observed volatility, steady income, access to large-scale platforms.

Cons: Potential redemption limitations during stress; no opportunity to purchase at a discount to NAV.

Institutional Commingled Funds / Separate Accounts (SMAs)

Examples of Certain Managers: Ares, HPS, Golub, Churchill, Crescent

Liquidity: Illiquid; capital typically locked for 7–10 years.

Valuation: NAV-based with quarterly marks.

Access: Institutional investors (pensions, endowments, sovereign wealth funds, large family offices); minimums often \$10M+.

Fees: Generally 1–1.5% management plus 15–20% carry; large investors may negotiate fee concessions.

Transparency: Moderate—detailed quarterly reporting but no public filings.

Convexity: Moderate; ability to co-invest, structure bespoke financings, and access niche strategies may introduce asymmetric return potential.

Downside Protection: Strong alignment with GPs, bespoke covenants, and negotiated protections.

Pros: Access to differentiated transactions, co-investments, structural protections.

Cons: Illiquidity and J-curve effects; limited accessibility for smaller investors.

Secondary Fund Purchases

Examples of Certain Managers: Transactions facilitated by secondary managers such as Ardian, Collier, Lexington, StepStone

Liquidity (for sellers): Provides an exit mechanism for LPs prior to fund maturity.

Access (for buyers): Ability to acquire seasoned portfolios, often at discounts to NAV.

Valuation: Negotiated pricing based on portfolio quality, GP reputation, and market conditions.

Fees: Buyers assume existing fund economics; in certain cases, terms may be partially renegotiated.

Transparency: Variable, depending on GP cooperation and available information rights.

Convexity: Moderate to high; discounted purchases may enhance IRRs and introduce optionality.

Downside Protection: Discounts function as a margin of safety, similar to public BDC purchases below NAV. Seasoned portfolios also mitigate J-curve risk and enhance return visibility.

Pros: Immediate cash yield, J-curve mitigation, potential discounts.

Cons: Limited ability to alter portfolio composition; competitive pricing environment.

Comparative Overview

FEATURE	Public BDCs	Private BDCs / Interval Funds	Institutional Funds / SMAs	Secondary Fund Sales
Liquidity	Daily trading	Quarterly redemption (limited)	Locked 7–10 yrs	Exit liquidity for sellers; buyers locked
Access	Retail investors	HNW via wealth platforms	Institutions only	Institutional/qualified buyers
Valuation	Market-driven, NAV \pm premium/discount (currently ~10% avg discount, with some >20%)	NAV-based, quarterly	NAV-based, quarterly	Negotiated (discount/premium to NAV)
Volatility	High (public sentiment)	Moderate	Low (private marks)	Low once acquired; pricing reflects volatility
Fees	Mgmt + incentive + market dynamics	Mgmt + incentive + distribution	Institutional fee structures	Existing fund fees, may adjust
Transparency	Highest (public filings)	Moderate (quarterly reports)	Moderate (LP reports)	Variable (GP-dependent)
Convexity	Low-to-moderate; enhanced when bought at NAV discount (10–25% currently observed)	Low–Moderate	Moderate	Moderate–High

Source: Bloomberg market prices, March 13, 2026

Downside Protection	Enhanced when bought below NAV (10–25% cushion)	Moderate (NAV smoothing, gates)	Strong (alignment, covenants)	Enhanced through discounts and seasoned portfolios
Return Profile	8–12% dividends, volatile	8–10% steady income	8–12% IRRs (gross), co-investments	Enhanced IRRs if discounted; immediate yield
Best Fit	Retail seeking yield + liquidity	HNW seeking steady income	Large institutions needing scale	Institutions seeking J-curve mitigation + discounts

Overview: Public BDC Discounts vs. Secondary Purchases

Case Example: Ares Capital (ARCC) vs. Ares Private Funds

ARCC, Ares' flagship public BDC, has historically traded near NAV but has periodically moved into 10–15% discounts during market volatility.

Investors purchasing during these windows gain exposure to Ares' origination pipeline with a built-in margin of safety. The portfolio could decline by the amount of the discount before impairing investor capital relative to purchase price, while dividend yields are enhanced.

This dynamic mirrors secondary fund purchases, where investors acquire seasoned portfolios at discounts—mitigating the J-curve while benefiting from both income and potential re-rating. Both structures embed convexity and downside protection, though one reflects public market pricing and the other private market negotiation.

Historical Context: Discounts Across Cycles

40–50%

Discount to NAV
(Public BDCs)

Global Financial Crisis (2008–2009)

Public BDCs traded at discounts exceeding 40–50% to NAV. Investors entering at those levels experienced amplified convexity as discounts narrowed during recovery.

6–8%

Discount to NAV
(Public BDCs)

COVID-19 Shock (2020)

Discounts widened to 30–40% before narrowing rapidly as liquidity returned, generating strong total returns over the subsequent 12–24 months.

20%

Average Discount
to NAV
(Public BDCs)

Current Environment (January 2026)

Average discounts are approximately 20%, with some names exceeding 25%. While not crisis-level dislocations, these discounts may provide a buffer against downside risk and offer re-rating potential if credit stability persists or rates decline. Historical precedent suggests that discount entry points can amplify convexity: widening discounts provide entry cushions, while narrowing discounts enhance total returns.

Key Takeaways & Implications

Public BDCs offer liquidity and accessibility, with their relative attractiveness increasing when trading at discounts to NAV. We see current discounts of ~20% on average—and 25–30% in certain cases— as a potential path to introduce both income enhancement and downside protection.

Private BDCs/interval funds offer stability but typically lack the embedded convexity of discount-driven entry points. Liquidity gates may dampen volatility but can constrain flexibility during periods of stress.

Institutional funds and SMAs provide strong structural alignment and moderate convexity, albeit with illiquidity and J-curve considerations.

Secondary purchases are thematically aligned with public BDC discounts: both involve acquiring exposure below NAV, embedding convexity and enhancing downside protection.

Conclusion

We believe that, in the current environment, public BDCs trading at discounts and secondary fund purchases represent compelling structural entry points into middle-market direct lending. While public BDCs have historically been associated with retail participation, both high-net-worth and institutional investors may benefit from their liquidity and embedded convexity, particularly when paired with larger secondary allocations.

Both public BDC discounts and secondary purchases introduce opportunities to acquire exposure at a margin of safety, enhancing convexity and supporting portfolio resilience across market cycles.

Private BDCs and interval funds should be avoided until the gaps in NAVs compared to public counterparts narrow, and/or investors achieve better visibility on current redemption trends from these vehicles.

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Sources

1. Bloomberg; As of March 13, 2026.

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