

BDC Analysts Spotlight Resilient Credit Trends and a Brighter 2026 Outlook at AICA's Inaugural Earnings Pulse Session

December 12, 2025

Despite noisy headlines around private credit, two of the industry's most seasoned analysts described the **third-quarter BDC earnings season as surprisingly stable**—even strong in several respects—during the Active Investment Company Alliance's first **"BDC Earnings Pulse"** conversation hosted on December 10, 2025.

The session, moderated by AICA founder and CEF Advisors President **John Cole Scott**, brought together **Nicholas Marshi**, publisher of The BDC Reporter, and **Mitchel Penn**, BDC analyst at Oppenheimer, for a data-rich discussion on earnings trends,

credit quality, spreads, valuations, and the outlook heading into early 2026.

Earnings Strength and a Narrowing Credit-Loss Trend

Penn opened with a headline that contradicts much of the recent market rhetoric: "ROE for the group was **9.4%** for the quarter, with NII margins flat and credit losses materially lower," he said.

Credit losses, which hit **246 bps in Q1**, declined sequentially throughout the year and were just **50 bps** in Q3. Year-to-date losses now total **135 bps**, roughly half of early-year expectations.

Penn also noted that BDC portfolios remain conservatively marked at about **96.4% of par**, implying embedded reserves of **3.6%**, and that current market valuations—many BDCs trading near **90% of book value**—look disconnected from improving credit data.

"The market is pricing in nearly 100 bps of Fed easing," Penn said, arguing that valuations already discount a more aggressive rate-cut path than the Fed seems to project.

Note: Current data mentioned by Mitchel in this article reflects BDCs under coverage except for one that has not reported. The data on 5-year ROE and dividend yield were as of Q2 2025.

NAV Trends Show a “Very Normal Quarter,” Not a Credit Shock

Marshi struck a similar tone. “It was a very normal quarter—almost dull—despite the negative headlines,” he said, highlighting that **more BDCs increased NAV per share this quarter than in any of the prior four quarters.**

A handful of weaker players continued to show stress, but no new systemic issues emerged.

Marshi emphasized that the barrage of negative private-credit commentary—particularly around a few high-profile defaults—has been **misapplied to BDCs.**

“Those defaults were broadly syndicated loans, not private credit. And the BDCs that owned them were the same BDCs that have struggled with credit historically.”

He also reminded investors that BDCs continue to demonstrate **remarkable consistency in credit outcomes,** with recent loss rates remaining below historical averages.

Understanding PIK, Non-Accruals, and What the Data Really Means

A significant portion of the discussion

focused on **payment-in-kind (PIK)** interest—one of the most misunderstood metrics in financial media.

Marshi clarified that not all PIK is distress-driven: “Some PIK is simply a structural choice. Some is part of a negotiated workout. Some indicates stress—and sometimes it doesn’t. You cannot make industry-wide conclusions from the aggregate PIK number.”

Penn agreed, explaining that meaningful PIK analysis requires **loan-level conversations with management,** reviewing cash vs PIK splits, and understanding whether PIK is **3% add-on income or 80% capitalized interest.**

He also reminded investors that BDCs incorporate unrealized losses immediately—one reason realized loss-tracking often lags reality: “If you only track realized losses, you’ll be six months late. Unrealized marks tell the story in real time.”

Valuations, Scale, and Why Yield ≠ Quality

Penn highlighted a critical misconception in retail investor behavior:

“Dividend yield is often a proxy for risk—not a proxy for value.”

His research shows:

- **Top-quartile BDCs:** 15.2% 5-year ROE, 8.8% dividend yield

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- **Bottom-quartile BDCs:** 4.3% ROE, 14% dividend yield

The takeaway: **High yield often signals a structurally riskier portfolio**, not an overlooked bargain.

Both analysts rejected the notion that large BDCs inherently outperform or underperform: “You can have excellent ROE at any size,” Penn said. “You can also have disappointing results at any size.”

Track records matter, but newer large-cap BDCs must be analyzed with care, especially when **private BDC fee structures** differ substantially from their listed versions.

Rates, Earnings Power, and the Setup for 2026

With the Fed cutting rates **25 bps** during the session, both analysts addressed the impact of lower base rates.

Lower rates:

- **Reduce stress** for portfolio companies that were near debt-service thresholds
- **Lower BDC income**, but in uneven ways
- Are **partially offset** by high levels of undistributed taxable income and earnings cushions already built up

Marshi noted BDCs “saw this coming from miles away” and have preserved dividend coverage for a potential lower-rate environment.

He also raised a major but under-reported tailwind: “There is a tremendous amount of equity sitting on BDC balance sheets. As private equity exits accelerate in 2026, BDCs can follow them to the cash register.”

Early signs of an M&A pickup are appearing in industry press, and BDC equity marks—many held for five or more years—could convert into meaningful realized gains next year.

Regulatory Catalysts: INVEST Act and AFFE Relief

The analysts briefly addressed two structural developments:

1. INVEST Act – Potential Removal of AFFE

Both agreed the removal of Acquired Fund Fees and Expenses (AFFE) could meaningfully lift institutional demand for BDCs.

Marshi called the multi-year effort “Waiting for Godot,” but noted that if finally enacted, it could provide **a powerful re-rating catalyst**.

2. Tax Parity for BDC Dividends

This proposal remains speculative but would significantly improve BDC after-tax yield relative to other income vehicles.

Sentiment, Tax-Loss Selling, and Near-Term Setup

Audience question about whether tax-loss selling pressure was largely behind the sector, Marshi said he would “assign a **60% probability** to a Santa Claus rally.”

CEF Advisors’ own BDC indices show about:

- 1-month returns up ~5%
- 3-month returns down ~3%—a snapshot of the pendulum shift in sentiment through November and early December.

Final Thoughts

Penn closed with a reminder: “Focus on ROE—not dividend yield. Stocks trade on earnings.”

Marshi ended on an optimistic note for 2026: “The long-awaited private-equity realization cycle may finally be at hand. Many BDC portfolios are positioned to benefit.”

Scott encouraged attendees to share the session replay once released and noted that

AICA expects to host the next Earnings Pulse discussion in **90 days**.

Replay video session available on <https://aicalliance.org/events/>

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