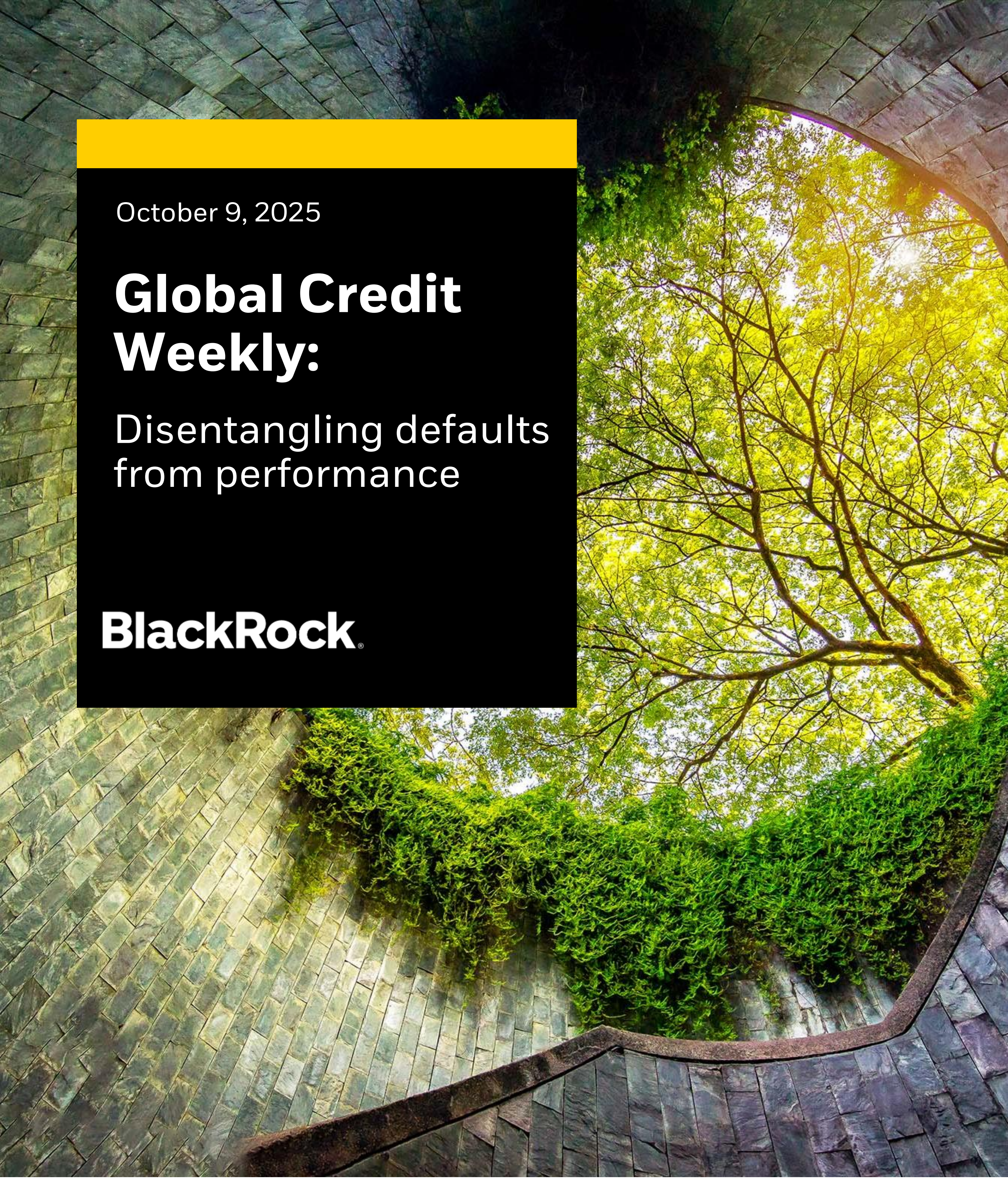

October 9, 2025

Global Credit Weekly:

Disentangling defaults from performance

BlackRock

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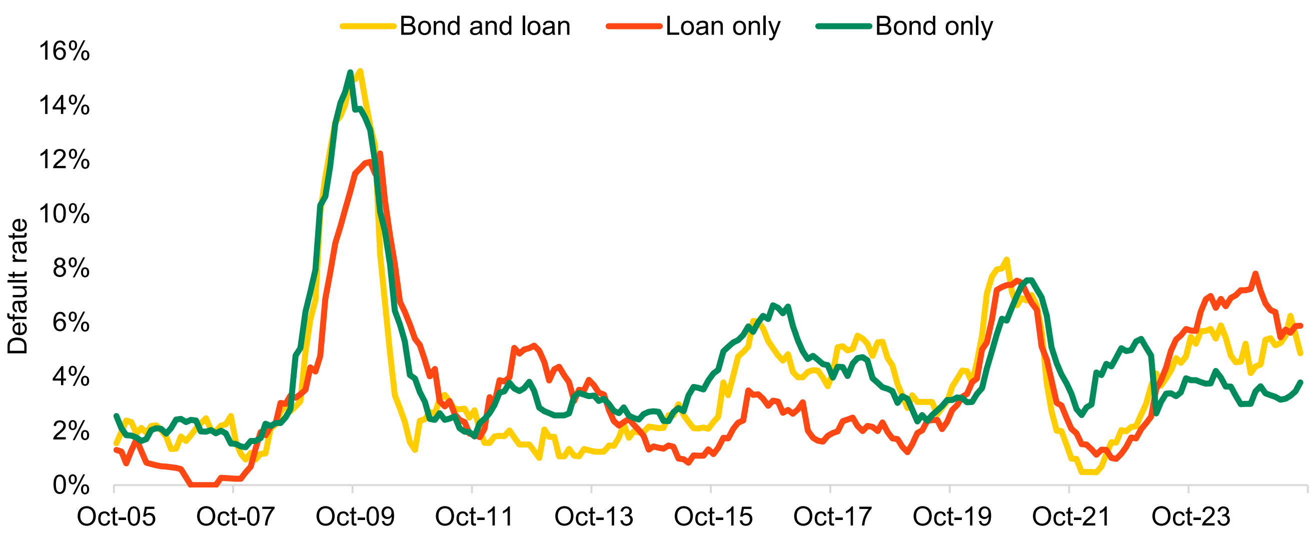
Key takeaways

- Recent idiosyncratic headlines have refocused some market participants on default trends in the liquid and private credit markets, and whether a new peak in defaults is on the horizon. As we outlined in our *4Q2025 Global Credit Outlook*, we believe the peak in corporate default activity is likely behind us, driven by a combination of 'supportive enough' economic growth, moderating debt service costs, and corporates' demonstrated ability (so far) to navigate a dynamic backdrop with resilience, owing to a myriad of operational levers at their disposal.
- That said, we expect dispersion to remain a defining feature of the investing landscape, as some firms may still have difficulty 'growing into' debt capital structures formed in an ultra low-interest rate environment. We expect this to be most pronounced for firms with exposure to some of the most pressured end markets, such as younger, subprime consumers with various forms of debt (a cohort which generally hasn't benefited from gains in home prices or equity markets). We believe this underscores the importance of credit selection, underwriting and workout expertise.
- The key question for investors, in our view, is whether pockets of stress warrant an outright defensive stance towards corporate credit risk. We do not believe such a posture is justified at this stage and remain comfortable *selectively* moving down in credit quality – a view we have held since April 10th. We continue to prioritize income and yield in corporate credit, as opposed to the potential for a total return 'boost' from tighter spreads or lower interest rates (fixed rate duration).
- In this *Global Credit Weekly*, we disentangle default activity from corporate credit performance – again highlighting the resilience of the lower-rated portions of the USD and EUR corporate credit markets. We also revisit four of the key 'default themes' we have previously highlighted, including trends across capital structure type, company sizing, distressed exchanges, and repeat defaulters. We also unpack some of the nuances related to the definition of a 'default' across liquid and private credit markets, and underscore why we focus more on realized losses.

Exhibit 1: Default rates across the capital structure are converging, as rates normalize
Issuer-weighted, trailing 12-month default rates for the global universe of issuers tracked by Moody's. Default rates include distressed exchanges and payment defaults.



Source: Moody's, BlackRock. As of August 31, 2025 (most recent available as of October 8, 2025).

Disentangling defaults from performance

Recent idiosyncratic headlines have refocused some market participants on default trends in the liquid and private credit markets, and whether a new peak in defaults is on the horizon. As we outlined in our *4Q2025 Global Credit Outlook*, we believe the peak in corporate default activity is likely behind us, driven by a combination of 'supportive enough' economic growth, moderating debt service costs, and corporates' ability (so far) to navigate a dynamic backdrop with resilience. That said, we expect dispersion to remain a defining feature of the investing landscape, as some firms may still have difficulty 'growing into' debt capital structures formed in an ultra low-interest rate environment. We believe this underscores the importance of credit selection, underwriting and workout expertise.

The key question for investors, in our view, is whether pockets of stress warrant an outright defensive stance towards corporate credit risk. We do not believe such a posture is justified at this stage and remain comfortable *selectively* moving down in credit quality – a view we have held since April 10th. Exhibits 2 and 3 illustrate the relative resilience of the lower-rated pockets of the USD and EUR corporate credit markets.

Exhibit 2: Lower-rated USD credit has demonstrated resilient performance, year-to-date

Year-to-date total returns (%) for various USD corporate credit indices

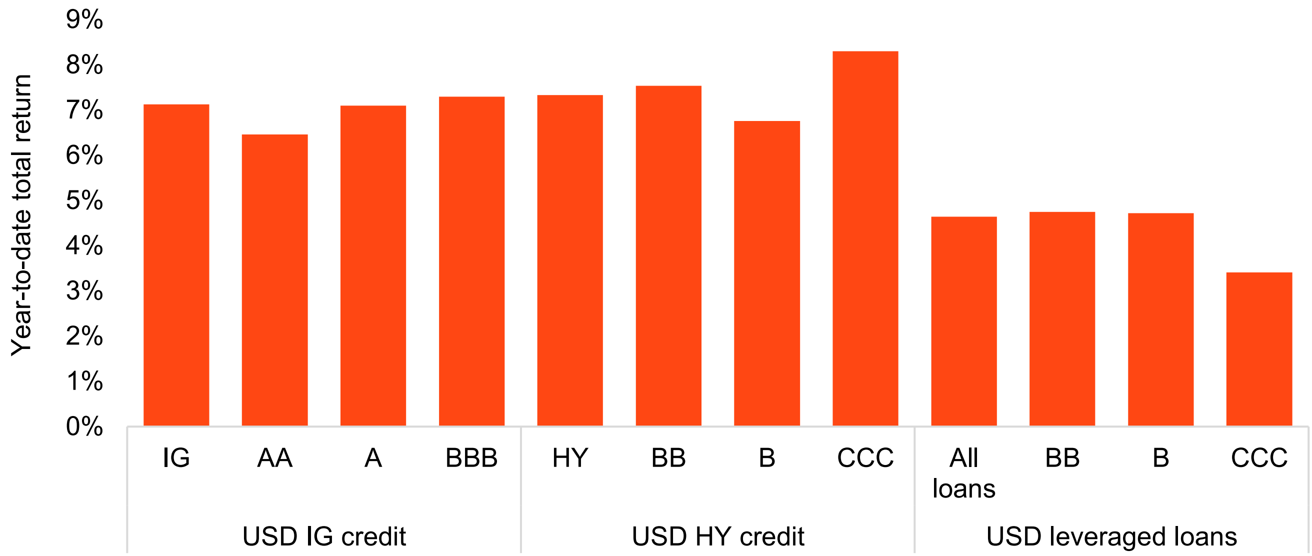
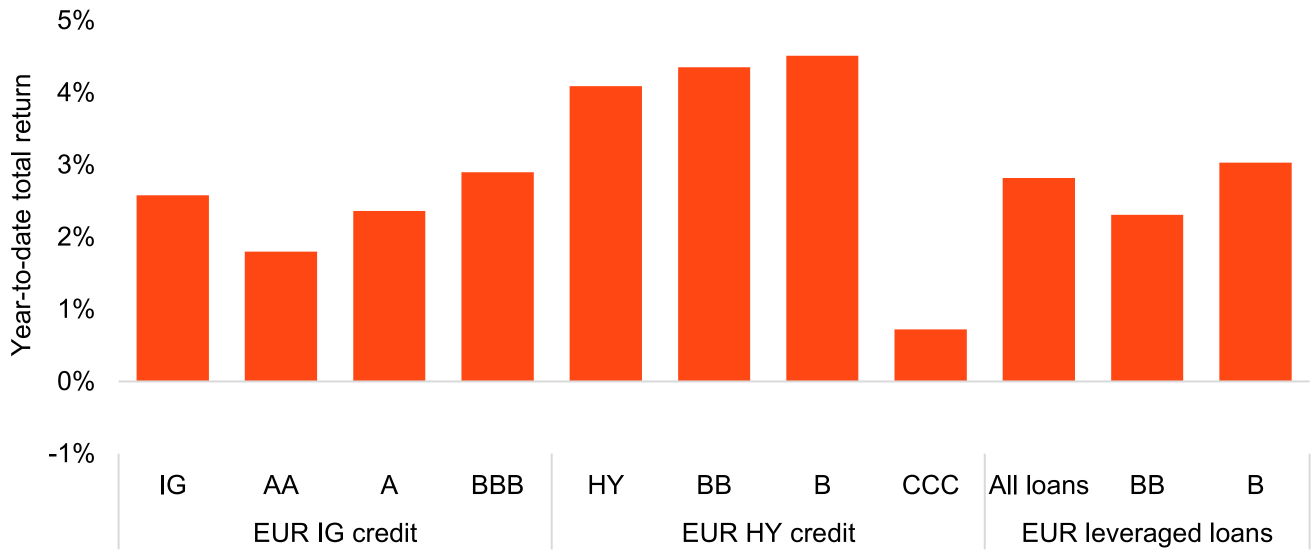


Exhibit 3: EUR HY has outperformed its higher-rated IG peer, year-to-date

Year-to-date total returns (%) for various EUR corporate credit indices



Source for both charts: Bloomberg, PitchBook LCD, BlackRock. As of October 8, 2025. **The figures shown relate to past performance. Past performance is not a reliable indicator of current or future results.** Index performance returns do not reflect any management fees, transaction costs or expenses. Indices are unmanaged and one cannot invest directly in an index.

Taking stock of the key 'default themes'

Nearly one year ago, we highlighted four 'default themes' visible across corporate credit markets: (1) smaller firms were defaulting at a higher rate than larger peers, (2) leveraged loan defaults were outpacing HY bond defaults, (3) distressed exchanges represented a larger share of overall default activity, and (4) an elevated share of default activity was attributed to 'repeat defaulters.'

While these trends are still largely in place, they are showing some signs of moderation. We view this pattern, coupled with a 'supportive enough' growth backdrop and an overarching theme of corporate resilience, as an indication that default activity may have passed its peak for this cycle.

Theme 1: Smaller firms are defaulting at a higher rate

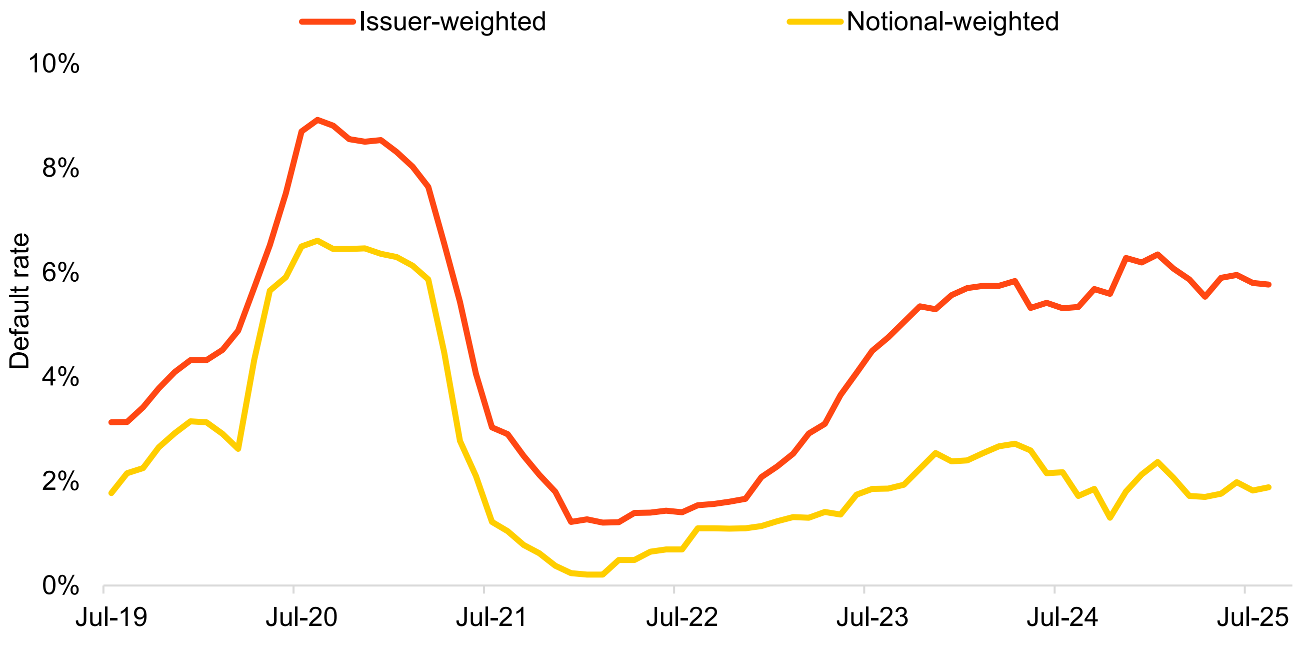
To start, Exhibit 4 demonstrates last-twelve-month (LTM) default rates on an issuer-weighted and notional-weighted basis for the firms in the syndicated markets (including USD HY bonds and leveraged loans) tracked by Moody's. Notably, smaller companies continue to conduct default activity at a higher rate than larger ones, as illustrated by the elevated issuer-weighted default rate.

A similar pattern is evident in private credit markets, as indicated by data from the Lincoln International Proprietary Private Market database, which captures a universe of approximately 6,250 U.S. portfolio companies. Indeed, the smallest borrower cohort (i.e., borrowers with less than $10 million in annual EBITDA) has experienced a higher size-weighted covenant default rate than other size cohorts over recent years (Exhibit 5, next page). (Note: as we discuss later, there are important definitional differences between the payment default / distressed exchanges shown in Exhibit 4 and the covenant defaults in Exhibit 5).

This theme of dispersion is nothing new. Depending on the industry, some smaller companies have faced greater challenges in navigating a backdrop of structurally higher interest rates and elevated inflation in recent years. They may not have the same magnitude of financial flexibility, business model diversification, or economies of scale as their larger peers, for example.

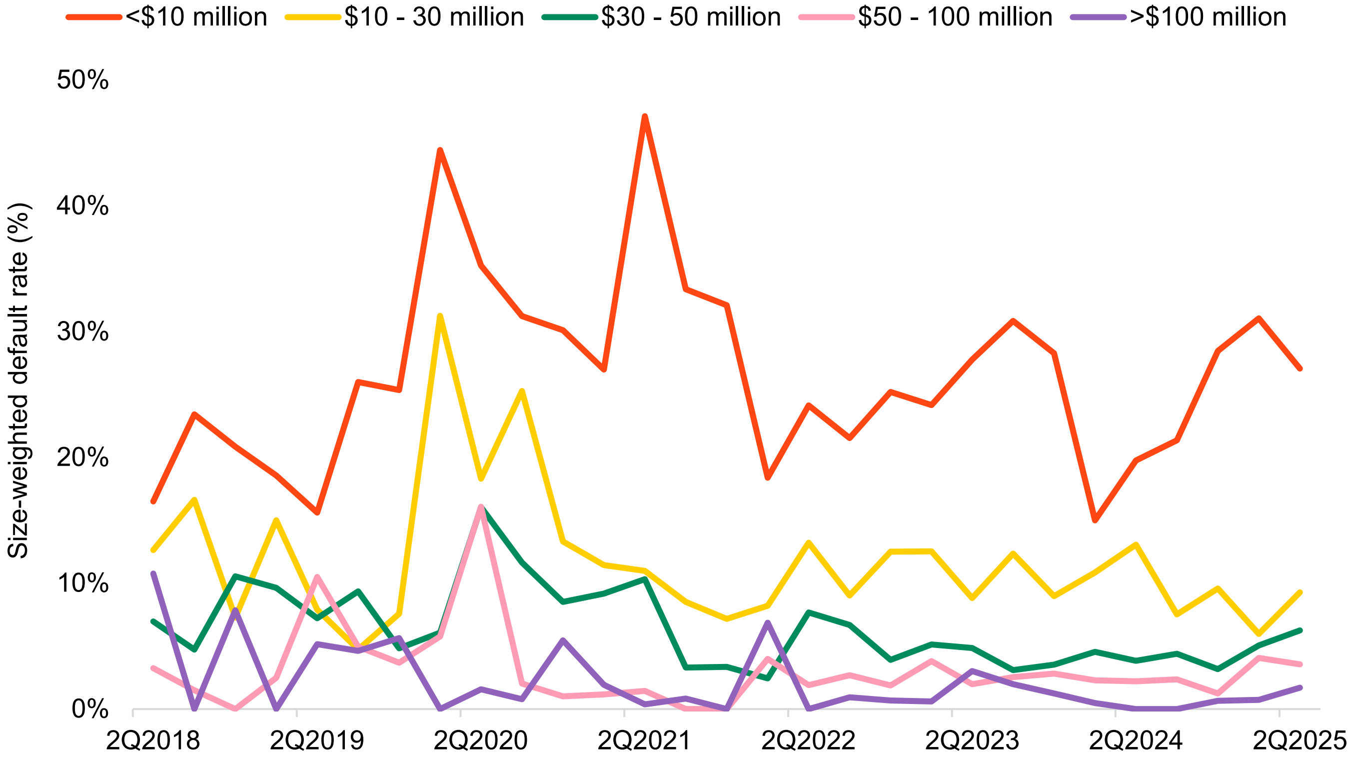
Exhibit 6 (next page) illustrates year-over-year (YoY), LTM adjusted EBITDA growth for companies in the Lincoln International Proprietary Private Market database. Notably, larger companies have managed to grow EBITDA at a faster pace than smaller peers over the last three years. This, in our view, underscores the importance of underwriting and credit selection when investing in corporate credit.

Exhibit 4: Moody's data suggests smaller issuers continue to drive default activity
Issuer-weighted and notional-weighted trailing 12-month default rates for the universe of USD leveraged loans and HY bonds tracked by Moody's. Includes distressed exchanges and payment defaults.



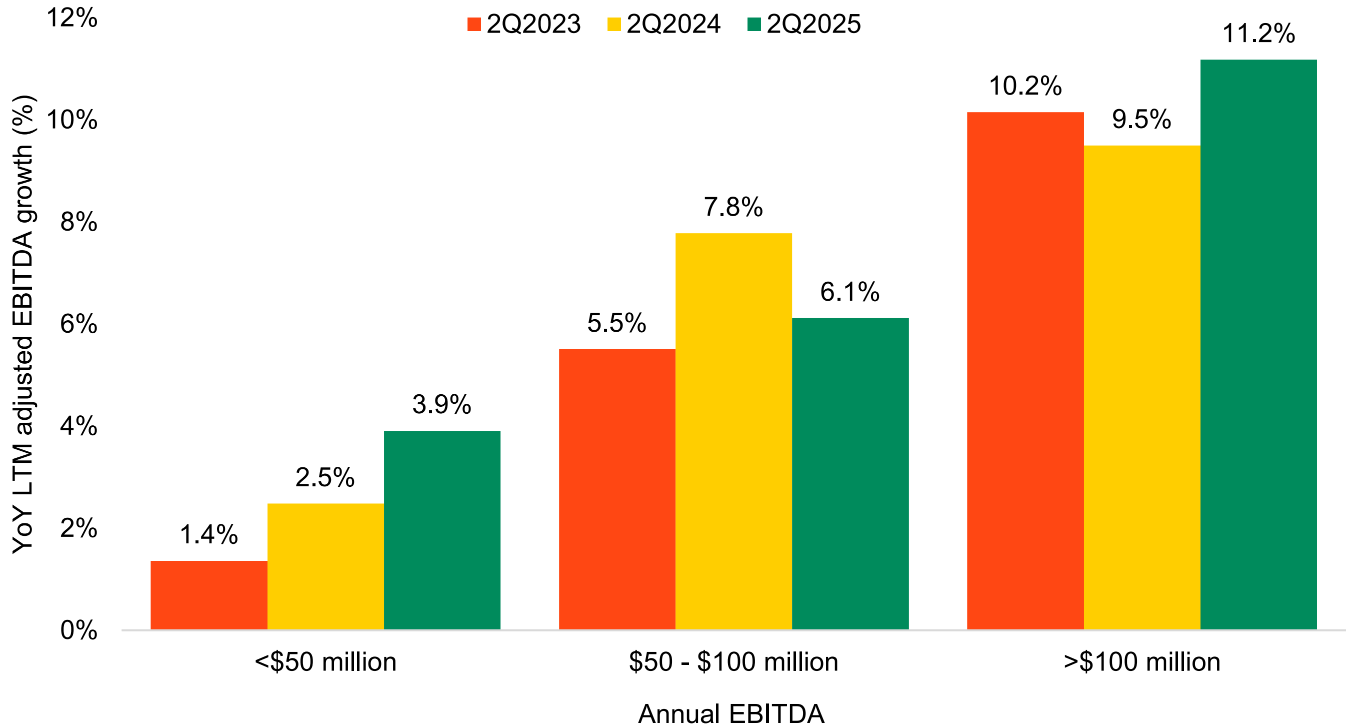
Source: Moody's, BlackRock. As of August 31, 2025 (most recent as of October 8, 2025).

Exhibit 5: The smallest borrower cohort has generated the highest covenant default rates
Covenant default rates (size-weighted, by annual EBITDA) for U.S. portfolio companies in the Lincoln International Proprietary Private Market Database



Source: Lincoln International Valuations & Opinions Group Proprietary Private Market Database, BlackRock. As of 2Q2025. Note: A default is defined as a covenant default (not necessarily a monetary default). The analysis is based on a size-weighted approach, which considers the total net debt balance for each of the portfolio companies that had a defaulting security in the respective quarter.

Exhibit 6: Larger companies have generated higher EBITDA growth in recent years
Year-over-year last twelve month (LTM) adjusted EBITDA growth, by annual EBITDA



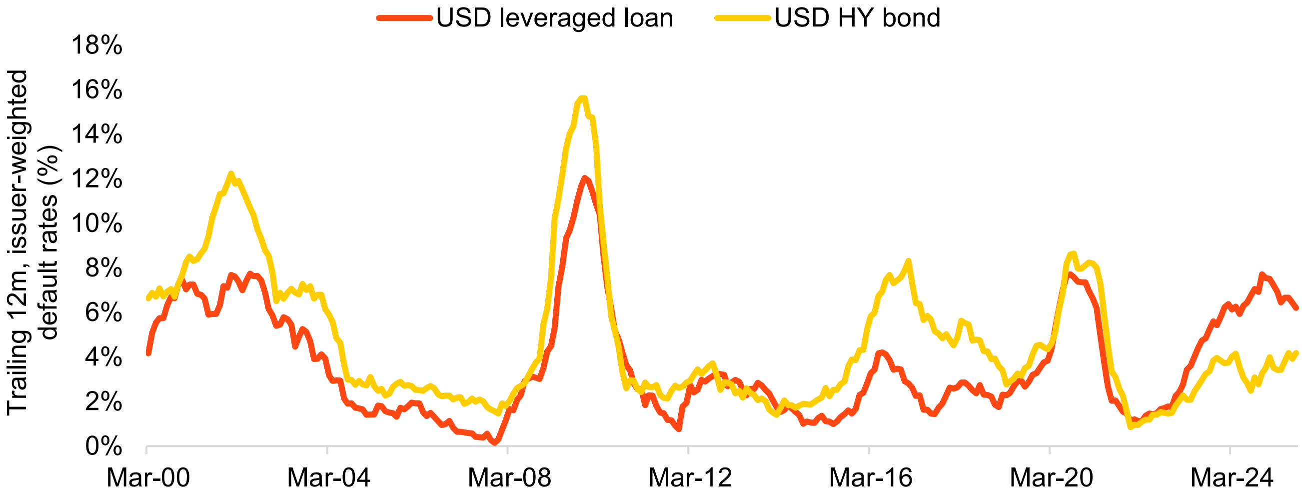
Source: Lincoln International Valuations & Opinions Group Proprietary Private Market Database, BlackRock. As of 2Q2025.

Theme 2: Leveraged loan defaults are outpacing HY bonds, but the gap is narrowing

Default rates for the USD leveraged loan market continue to outpace those of USD HY bonds, a trend that has been in place since early 2022 (Exhibit 7). But while the gap in defaults between USD loans and bonds reached record levels in November 2024, it has since compressed. Exhibit 1 echoes this trend using global data, showing that capital structures containing loans have experienced elevated default rates vs. bond-only capital structures in recent years. But again, default rates are converging.

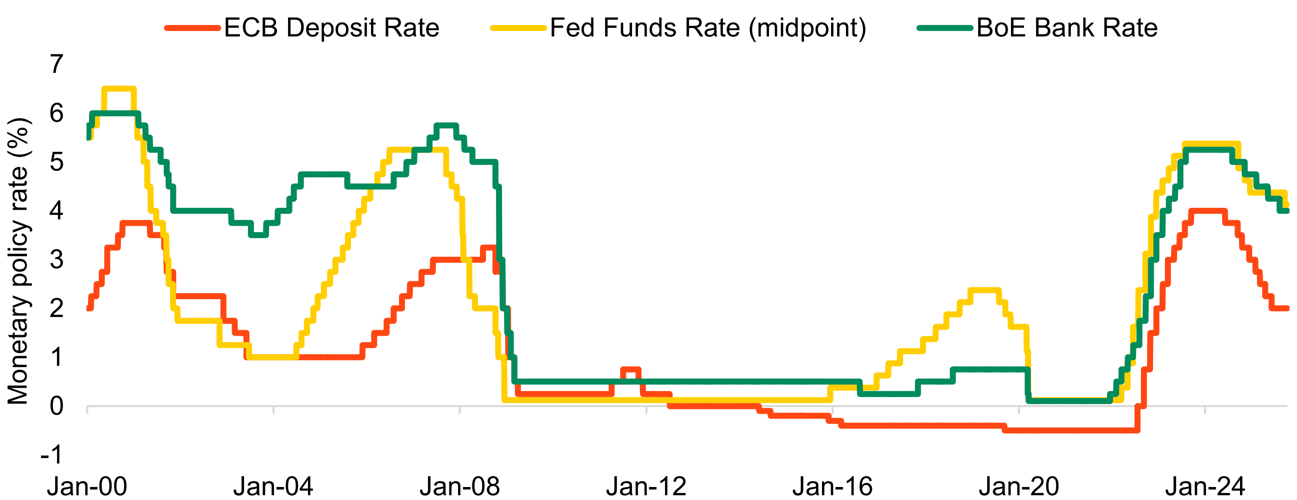
As we have highlighted previously, the differential between loan and bond defaults was driven, in large part, by the global rate hiking cycles of many developed market central banks in 2022-2023. While USD leveraged loan (i.e., floating rate) borrowers absorbed higher financing costs in real time, USD HY bond (i.e., fixed rate) borrowers encountered higher rates (at a different part of the curve), over time (i.e., if/when they chose to refinance low coupon debt). But as the rate cuts of 2024-2025 have been delivered (Exhibit 8), and interest rates have normalized, floating rate borrowers have received some relief from elevated borrowing costs. As such, we see scope for additional convergence between the loan and bond default rates as the interest rate backdrop further normalizes and as the impact of previous rate cuts is reflected.

Exhibit 7: The gap between default rates has converged from the local wides
Trailing 12-month, issuer-weighted default rates for the universe of USD HY bonds and USD leveraged loans tracked by Moody's. Includes distressed exchanges and payment defaults.



Source: BlackRock, Moody's. As of August 31, 2025 (most recent available as of October 8, 2025).

Exhibit 8: Global central banks have eased the degree of restriction in monetary policy
Monetary policy rates for the European Central Bank, Federal Reserve, and Bank of England



Source: BlackRock, European Central Bank, Federal Reserve, Bank of England, Bloomberg. As of October 7, 2025.

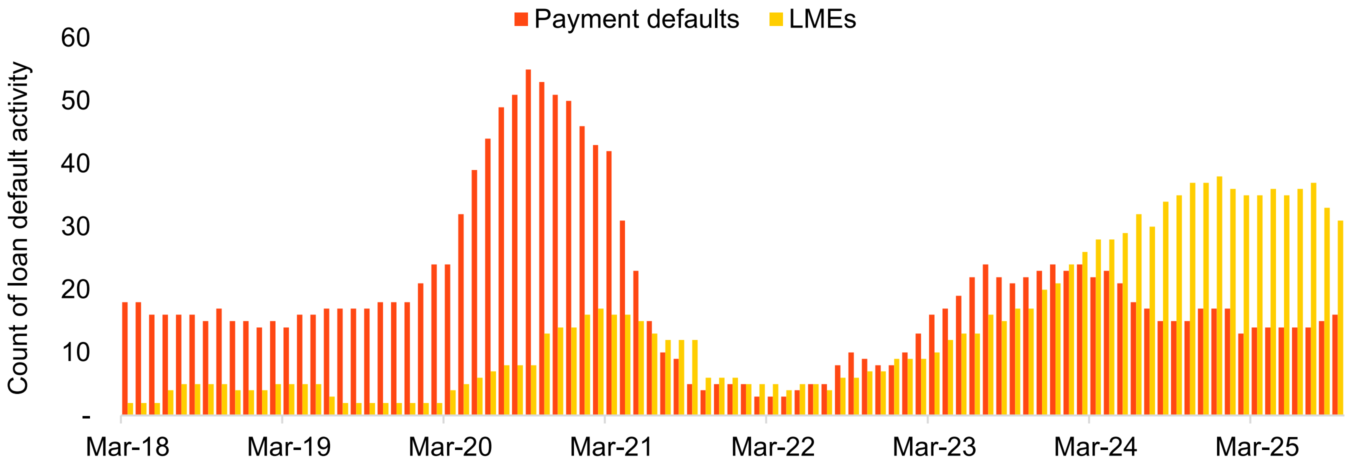
Themes 3 and 4: Liability management exercises represent a large share of default activity, and the trend of 'repeat defaulters' persists

Liability management exercises (LMEs) have become an important tool for stressed borrowers in the syndicated markets. Exhibit 9 demonstrates their growth over time in the USD leveraged loan market, with the trailing 12-month (TTM) count of LMEs outpacing that of payment defaults for most of 2024 and 2025.

That said, 'repeat' default activity suggests that these LMEs, in many cases, have not resolved stress in the capital structure on a sustainable basis. Exhibit 10 illustrates the share of LME transactions that return with a payment or bankruptcy default within the three subsequent years. 44% of 2022 LMEs and 24% of 2023 LMEs (so far) have returned for a payment or bankruptcy default.

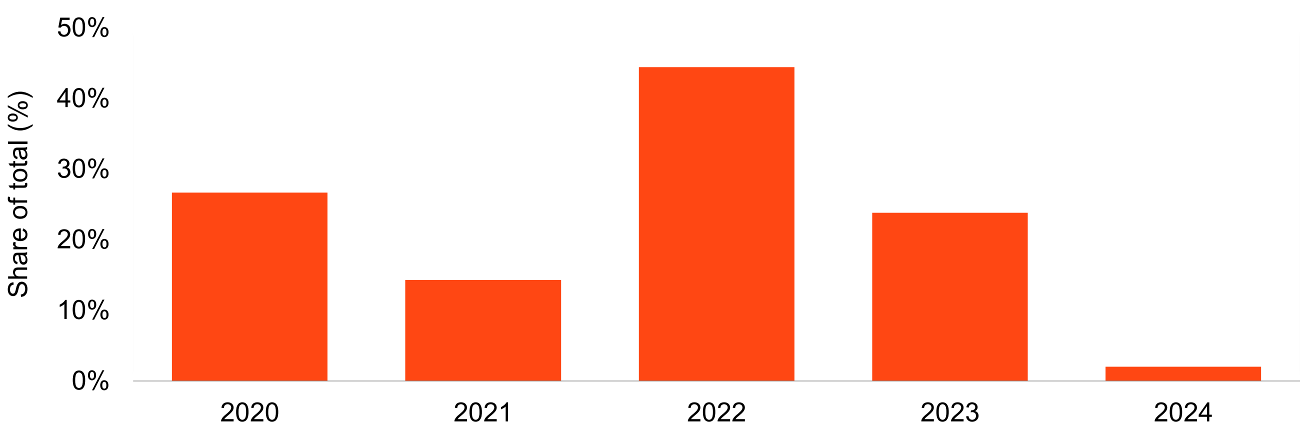
Recent data suggests the pace of LME transactions may be slowing from last year's record level. Indeed, the TTM count of LMEs in the USD leveraged loan market has declined to the lowest level since July 2024. Data from JP Morgan also notes that LMEs and distressed exchanges have accounted for 51% of total default/distress exchange volume in the USD syndicated market (including both leveraged loans and HY bonds), compared to a record of 68% in 2024, and a long-term average of 22%. And given their tendency to lead to repeat defaults in recent years, fewer LME activities could suggest fewer default actions ahead.

Exhibit 9: LMEs continue to outpace payment defaults
Count of trailing twelve-month defaults for USD leveraged loans, by default activity type (payment defaults and liability management exercises)



Source: PitchBook LCD, Morningstar / LSTA USD Leveraged Loan Index, BlackRock. Data through September 30, 2025.

Exhibit 10: 24% of companies that conducted an LME in 2023 have already returned with a payment or bankruptcy default
Share of LME transactions (by LME year) that returned with payment or bankruptcy defaults within the subsequent three years



Source: PitchBook LCD, BlackRock. Data through August 31, 2025 (most recent available).

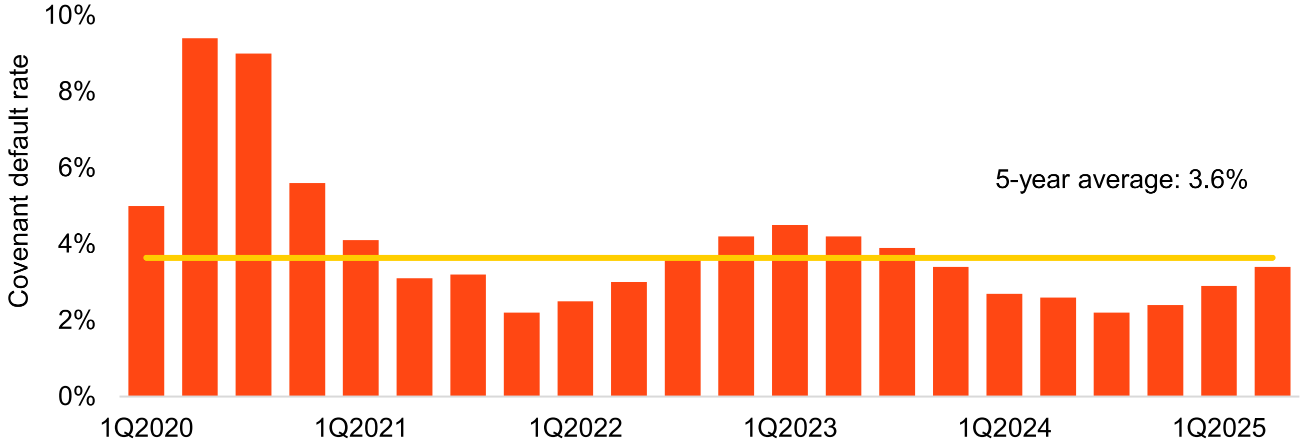
Private credit trends (and 'default' definition nuances)

Within private credit, we have documented modest signs of stress over recent quarters, though these remain largely contained – like the backdrop in liquid credit. For example: the Lincoln International Proprietary Private Market Database shows that covenant default rates for private credit loans have increased over the last three quarters, after several quarters of improvement in 2023-2024 (Exhibit 11).

Importantly, in private credit, a 'default' can often refer to a *covenant* default, which does not necessarily mean that a borrower missed an interest payment or that a lender incurred a financial loss. Rather, it often serves as an early warning signal, prompting collaboration between the borrower and lender to address emerging stress. The presence of maintenance covenants enables this process and is different from the syndicated credit market, which is largely classified as 'covenant lite.'

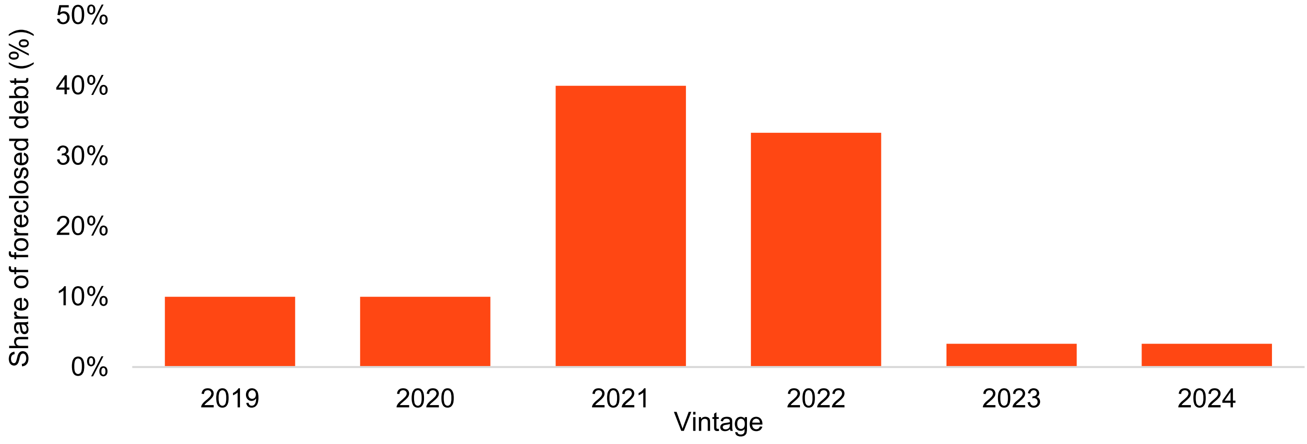
Away from defaults, Lincoln International details that private credit foreclosures have also risen, totaling $20.7 billion in 1H2025, up from $8.1 billion in FY2024. Lincoln defines 'foreclosed' debt as situations where lenders have taken control of a company or expect to do so imminently. As shown in Exhibit 12, more than 70% of 2025 foreclosed debt was attributed to 2021 and 2022 vintage loans, most of which were underwritten in a much lower interest rate environment (again, Exhibit 8). We see this increase in foreclosure activity as evidence that private credit lenders are actively addressing instances of portfolio stress, rather than a sign of widespread deterioration.

Exhibit 11: Defaults have increased for three consecutive quarters, but remain modest
Aggregate size-weighted covenant default rate, and the 5-year historical average, for the U.S. portfolio companies included in the Lincoln International Proprietary Private Market Database



Source: Lincoln International Valuations & Opinions Group Proprietary Private Market Database, BlackRock. As of 2Q2025. A default is defined by Lincoln as a covenant default (not necessarily a monetary default). The calculation is size-weighted and considers the total net debt balance for each of the portfolio companies that had a defaulting security in the respective quarter.

Exhibit 12: 2021 and 2022 vintage debt represented the largest share of foreclosures this year
Percent of debt foreclosed in 2025 by vintage, using the Lincoln Proprietary Private Market Database



Source: Lincoln International Valuations & Opinions Group Proprietary Private Market Database, BlackRock. As of 2Q2025. Data considers senior and unitranche term loans.

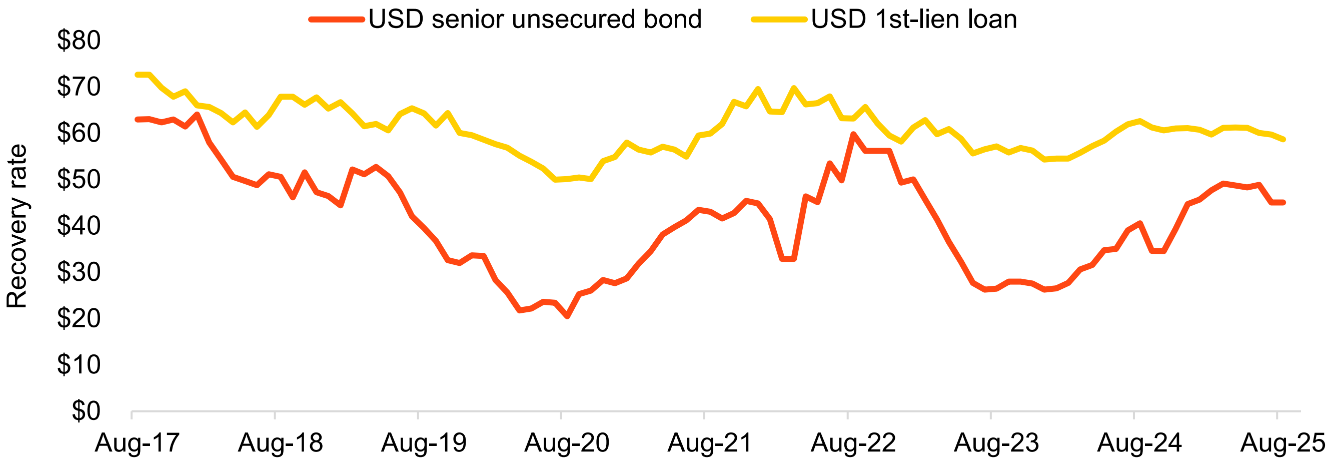
Differentiating between defaults and losses

Across syndicated and private credit markets, the severity of a default is a key consideration when assessing the potential impact to performance. And a key factor in determining the severity is the recovery rate.

Exhibit 13 demonstrates recovery rates for senior unsecured bonds and first lien loans, again using the syndicated universe tracked by Moody's. As of August 2025, recovery rates for USD leveraged loans remained above those of HY bonds, extending the longer-term historical trend. This reflects, in large part, the senior secured position that leveraged loans hold in capital structures.

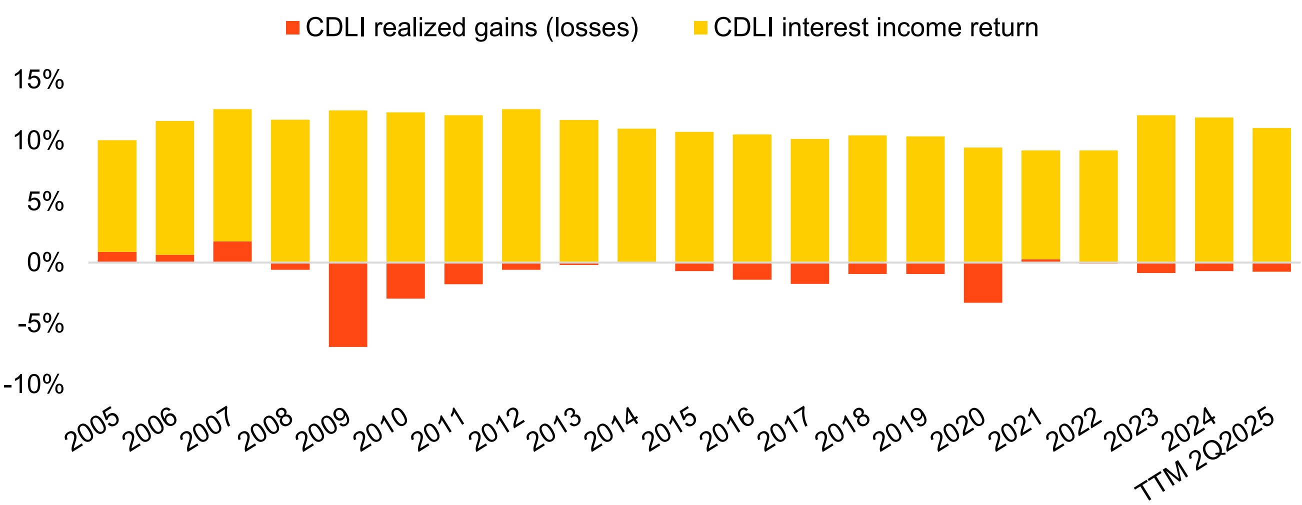
In private credit, we focus more on realized loss rates (as opposed to covenant defaults), when assessing the potential impact to performance. Data from the Cliffwater Direct Lending Index (CDLI), an index of over 20,000 USD middle market loan holdings representing over $485 billion in assets under management (AUM), suggests that TTM losses remain contained relative to interest income (Exhibit 14), even as covenant defaults have ticked up (again, Exhibit 11).

Exhibit 13: USD leveraged loan recovery rates continue to outpace those of USD HY bonds
Trailing 12-month USD first lien loan vs. USD senior unsecured bond recovery rates (per $100 par)



Source: Moody's, BlackRock. As of August 31, 2025 (most recent available as of October 8, 2025). Measured by debt prices, which are taken immediately prior to distressed exchanges or 30 days after non-distressed exchange defaults.

Exhibit 14: Losses for private credit remain contained, even as covenant defaults increased
Trailing 12-month income return and realized gains (losses) for the Cliffwater Direct Lending Index



Source: Cliffwater Direct Lending Index, BlackRock. As of June 30, 2025. Realized gains can be driven by equity stubs, warrants, and gains on exited investments. These were more common in 2005-2007, when second lien and mezzanine loans were a greater portion of the CDLI. **The figures shown relate to past performance. Past performance is not a reliable indicator of current or future results.** Index performance returns do not reflect any management fees, transaction costs or expenses. Indices are unmanaged and one cannot invest directly in an index. We exclude unrealized gains and losses in this chart. Long-term unrealized gains (losses) are approximately zero, as they either convert to net realized losses upon a credit default, or are reversed when principal is fully repaid.

A 'supportive enough' macro suggests the default peak has likely passed

While defaults often signal stress at the company level, they can also reflect broader macroeconomic pressures, such as sectoral headwinds or exposure to weaker segments of the consumer economy.

Exhibit 15 demonstrates the YTD count of default activity by industry for the USD syndicated markets (including leveraged loans and HY bonds). Some sectors had more meaningful contributions than others, potentially driven by macro headwinds such as policy changes or exposure to select consumer segments.

The key question for investors, in our view, is whether pockets of potential stress warrant an outright defensive stance towards corporate credit risk. We do not believe such a posture is justified at this stage. For example, with growth poised to potentially reaccelerate in 2026 and borrowing costs becoming incrementally less onerous (at least for floating rate borrowers), we feel comfortable that the peak in defaults for this cycle is likely behind us. For context, as of October 7th, the Atlanta Fed's GDPNow tracker estimated 3Q2025 real GDP at 3.8% - a level well above trend.

Distressed markers also point to stabilization

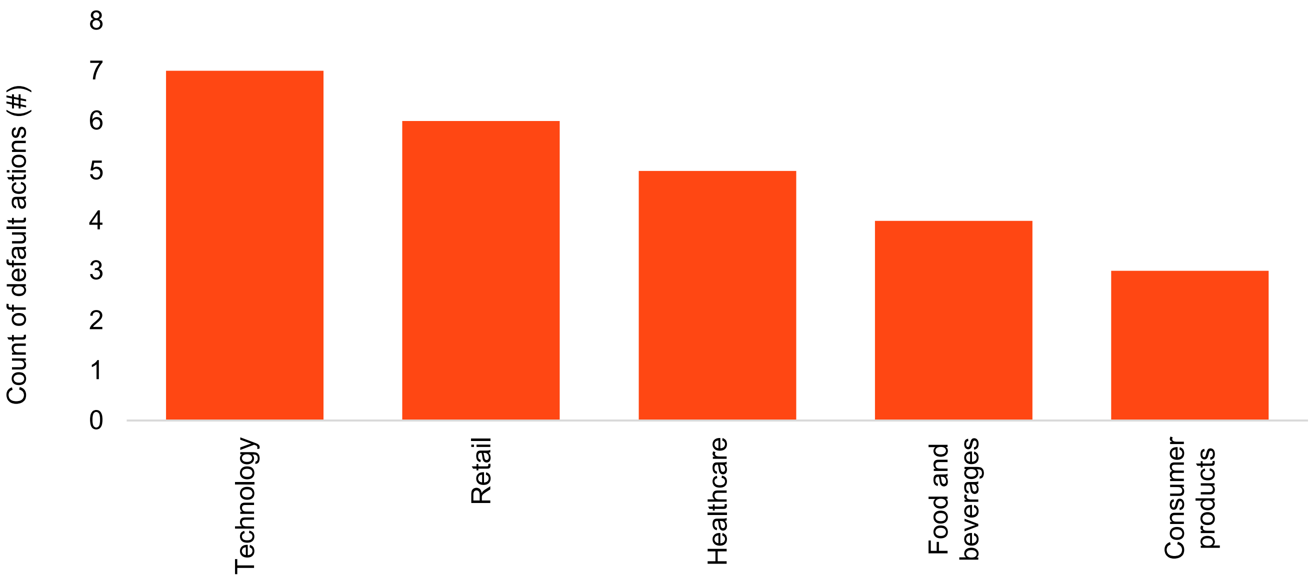
Beyond the potential for strong growth, which is supportive for corporate credit, common markers of distress also appear to have stabilized for credit markets.

Exhibit 16 demonstrates the rolling 3-month ratio of USD leveraged loan facility downgrades to upgrades, as tracked by PitchBook LCD. September marked the lowest ratio since April 2024, at 1.83x, suggesting that upgrades and downgrade activity are moving more in balance for leveraged loans. And in aggregate, the ratings backdrop has improved meaningfully from the local peak of 4.69x in February 2025.

Further, Exhibit 17 tracks the share of distressed facilities, by facility count, for USD leveraged loan and HY bond indices. Importantly, distress, as indicated by a loan priced below $80 and a bond spread greater than 1,000 basis points, does not always mean that a company will default. Distressed levels for both the leveraged loan and HY bond markets have trended downward since the series began in 2023. And while the level has been largely stable YTD for USD leveraged loans, the metric for HY bonds has fallen (improved) from the recent peak of April 2025. We view these incremental improvements as a further signal that syndicated credit markets are largely stable.

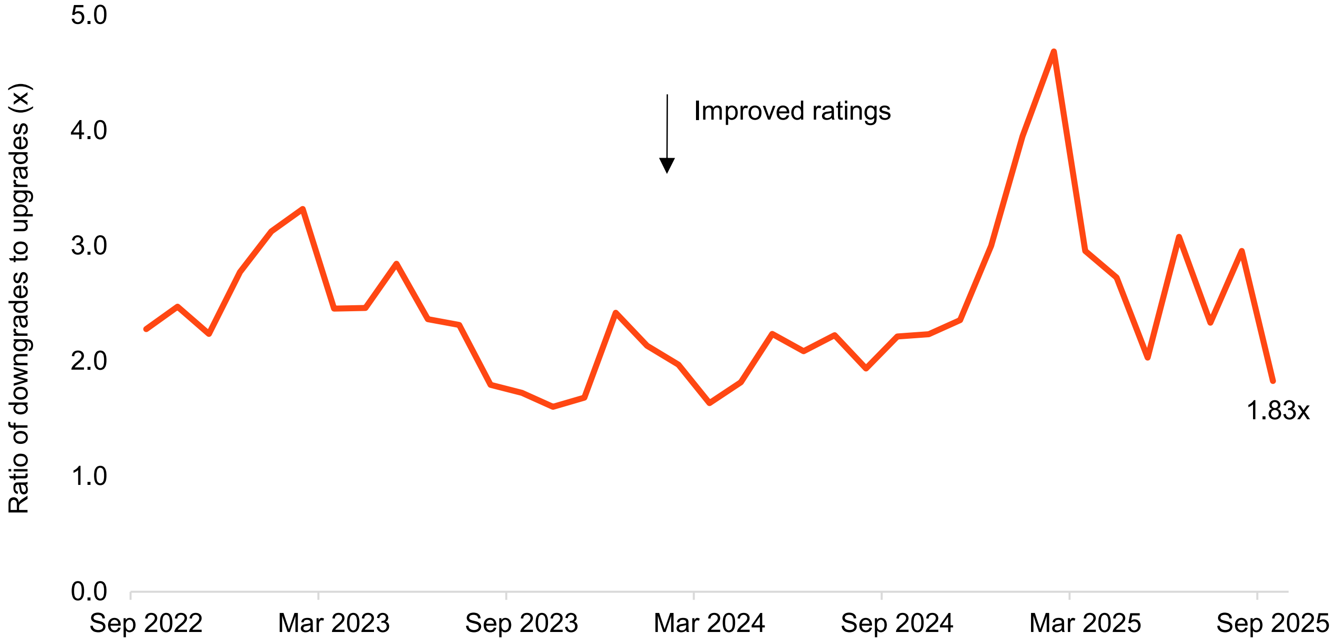
Exhibit 15: Certain sectors have led YTD default activity in syndicated markets

Year-to-date count of default activity (including payment defaults and distressed exchanges) by industry for the USD leveraged loan and HY bond markets



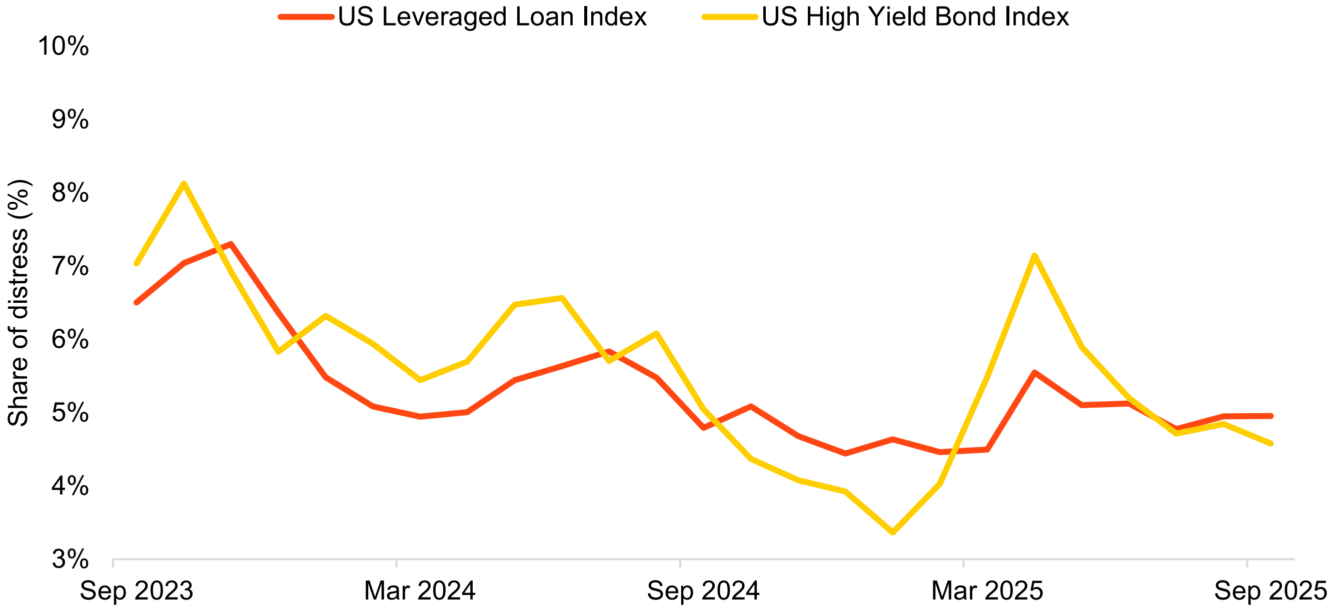
Source: JP Morgan, BlackRock. As of September 30, 2025. The following industries have 2 default actions: Automotive, Broadcasting, Chemicals, Financial, Gaming and leisure, and Services. The following industries have 1 default action: Cable and satellite, Industrials, Telecommunications, Transportation, and Utility.

Exhibit 16: The ratio of downgrades to upgrades has eased to its best reading since April 2024
Rolling three-month ratio of USD leveraged loan facility downgrades to upgrades, by count



Source: PitchBook LCD, Morningstar LSTA US Leveraged Loan Index, BlackRock. Data through September 30, 2025.

Exhibit 17: The distressed ratio has fallen for USD leveraged loans and HY bonds since 2023
Share of distressed facilities, by count, in the USD Leveraged Loan and the USD High Yield bond market



Source: PitchBook LCD, Morningstar LSTA US Leveraged Loan Index, S&P US High Yield Corporate Bond Index, BlackRock. As of September 2025. Captures percent of loans priced below $80 and percent of bonds with spreads above 1,000 basis points. Excludes defaults.

Unless otherwise stated, all reference to $ are in USD.

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Past performance is not a reliable indicator of current or future results and should not be the sole factor of consideration when selecting a product or strategy.

Changes in the rates of exchange between currencies may cause the value of investments to diminish or increase. Fluctuation may be particularly marked in the case of a higher volatility fund and the value of an investment may fall suddenly and substantially. Levels and basis of taxation may change from time to time.

Cliffwater Direct Lending Index (CDLI) is an index that assists investors to better understand private credit as an asset class. The CDLI seeks to measure the unlevered, gross of fees performance of U.S. middle market corporate loans, as represented by the underlying assets of Business Development Companies ("BDCs"), including both exchange-traded and unlisted BDCs, subject to certain eligibility criteria. The CDLI is an asset-weighted index that is calculated on a quarterly basis using financial statements and other information contained in the U.S. Securities and Exchange Commission ("SEC") filings of all eligible BDCs. Eligibility is set as all assets held by BDCs that (1) are regulated by the SEC as a BDC under the Investment Company Act of 1940; (2) have a substantial majority (approximately 75%) of reported total assets represented by direct loans made to corporate borrowers, as categorized by each BDC and subject to Cliffwater's discretion, and (3) file SEC form 10-Q (or 10-K, as applicable) within 75 (or 90) calendar days following the current Valuation Date. If a BDC meets the eligibility criteria, but has not filed its report on Form 10-K or 10-Q with the SEC at the time the index is reconstituted, asset information from its report will be included in the index at the time of the next reconstitution. This information is derived from sources that are considered reliable, but BlackRock does not guarantee the veracity, currency, completeness or accuracy of this information.

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