

The Complexity Premium

Why the Next Generation of Private Credit Returns Will Come from Cross-Border Origination, Not Direct Lending Scale

The Direct Lending Compression Problem

The U.S. private credit market has reached approximately \$1.5-2 trillion and now matches the broadly syndicated loan market in size. Moody's projects AUM exceeding \$2 trillion in 2026 and approaching \$4 trillion by 2030. This is a triumph of the asset class — and, increasingly, its biggest risk.

The sheer volume of capital chasing mid-market direct lending in the U.S. has compressed spreads, loosened covenants, and inflated adjusted EBITDA metrics to the point where many new vintages are underwriting risk that will not be apparent until the next default cycle. Vanguard's latest analysis notes that payment-in-kind income in direct lending portfolios has risen from ~4.2% pre-pandemic to 8.8% by Q3 2025 — a clear signal that borrowers are conserving cash by deferring interest, which is a polite way of saying they cannot afford to pay it.

Meanwhile, the five largest private credit managers — Apollo, Ares, Blackstone, Carlyle, and KKR — now manage a combined \$1.5 trillion in perpetual capital, representing roughly 40% of their total AUM. When the same five firms compete for the same deals, the result is not alpha. It is expensive beta with illiquidity risk.

Where the Structural Alpha Actually Lives

The opportunity is not in competing for the 500th U.S. sponsor-backed direct lending deal. It is in the markets where bank retrenchment has created genuine capital voids, structural complexity deters scaled competitors, and local origination capability is a prerequisite — not just a nice-to-have.

Three corridors stand out:

APAC private credit transactions typically offer a 300-400 basis point margin premium over comparable U.S. loans. This is not irrational pricing; it

reflects genuine structural complexity — diverse legal frameworks, less standardised documentation, thinner secondary markets, and currency management requirements. But for lenders with local origination capability, these are manageable risks that generate genuine excess return.

European mid-market credit, particularly in the fragmented Southern and Central European markets, offers 50–150 basis points of spread premium with historically lower default rates than the U.S. Carlyle’s 2026 outlook specifically identifies Europe as one of the most attractive markets for private credit, noting that local presence is critical to sourcing deals that fly under the radar of global allocators.

MENA and Africa represent the earliest-stage opportunity but the widest structural gap. Bank penetration is low, SME financing needs are enormous, and the regulatory environment is modernising rapidly (ADGM, DIFC, FSCA). The firms building origination platforms in these markets today will own the deal flow of the next decade.

The Origination Moat

In private credit, the moat is not capital. There is \$644 billion sitting in evergreen private credit vehicles alone as of mid-2025. The moat is the ability to originate proprietary deal flow in markets where scaled competitors cannot or will not operate.

This requires three things that capital alone cannot buy. First, local regulatory licenses and relationships — an ADGM license, an FSCA authorization, a MAS registration. These take 12–24 months to establish and create genuine barriers to entry. Second, local teams who understand borrower dynamics, collateral frameworks, and enforcement mechanisms in their jurisdiction. Third, structuring capability that bridges international investor expectations with local market realities — currency hedging, cross-border security packages, and investor reporting that meets institutional LP standards.

The firms that build these capabilities in 2026 will capture the structural alpha that has already been competed away in U.S. direct lending. The addressable market is enormous: Moody’s estimates the total potential addressable market for private credit exceeds \$30 trillion across all asset classes, with the fastest growth expected in EMEA and APAC.

The Stress Test

This thesis faces a real-time stress test. Credit spreads have widened sharply in March 2026 amid geopolitical shocks and the \$1.35 trillion maturity wall. BDCs are reporting increased borrower stress. The question for cross-border private credit is whether the complexity premium holds up under pressure — or whether it merely adds jurisdictional risk to already-elevated credit risk.

The answer depends on underwriting discipline. In the U.S., the combination of competitive pressure and abundant capital has degraded documentation quality to the point where high-profile credit issues trace back to weak covenants and inflated EBITDA adjustments. In less competitive markets, lenders can still negotiate meaningful structural protections: maintenance covenants, cash sweep mechanisms, board observation rights, and step-in provisions that have largely disappeared from U.S. direct lending.

Put differently: the cross-border complexity premium is also, paradoxically, a structural protection premium. Less competition means better terms.

Bottom Line

Private credit is not one market. It is a collection of markets at different stages of maturity, with radically different risk-return profiles. The U.S. direct lending market is mature, crowded, and increasingly priced for perfection. The real opportunity in the 2026–2030 vintage lies in building origination capability in the markets where capital is scarce, complexity is high, and the spread premium compensates for genuine risk rather than mere illiquidity. The investors who recognise this distinction — and deploy capital accordingly — will define the next era of private credit performance.