November 2022 Live Event-AICA Fall CEF/BDC/Interval Fund Bootcamp and Roundtable Panel #6; "Retail Access to Private Credit and Equity"

Wednesday, November 16, 2022

Aaron Filbeck, CAIA Managing Director and Head of UniFy, moderates the sixth panel of the AICA November 16th, 2022 live event; "Retail Access to Private Credit and Equity". Read the transcript below to hear the discussion among Mr. Filbeck and panelists Christian Munafo, Chief Investment Officer with Liberty Street Funds, Kevin Dockrell, CFA and Institutional Portfolio Manager with RBC BlueBay, Michael Grayson, Portfolio Manager with First Trust Capital Management, and Milwood Hobbs, Jr., Managing Director with Oaktree Capital Management.

Aaron Filbeck

Christian Munafo

Kevin Dockrell

Michael Grayson

Milwood Hobbs, Jr.

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Aaron Filbeck: Okay, we're going to go ahead and get started on panel number six called "Retail Access to Private Credit and Equity." I am joined by a great group of panelists this afternoon representing multiple asset classes across the private markets ecosystem and covering each of these different asset classes a little bit differently. We're going to focus primarily this afternoon on some macro discussions, some asset class-specific comments, and then we'll wrap up if there's time just talking a little bit about fund structure, just given that most of these individuals have some kind of interval fund or BDC or some other structure that's a little bit different than your traditional drawdown structure.

So I'm going to have each of these panelists introduce themselves, and then maybe just to start, just giving their observations on what they're seeing in their particular area of the market. And then we'll do some follow-up questions. So maybe I can just start with Millwood and just move. Go ahead, Christian, you can start.

Christian Munafo: Hi everyone, nice to be here and great to be with the panelists. My name is Christian Munafo, I'm the chief investment officer of Liberty Street Funds and a portfolio manager of the Private Shares Fund. Based on the last panel, I guess we're probably the most controversial group here because we do venture and growth investing in the private markets. We've been doing it through an interval fund for nearly a decade, we have a fund that we've scaled from about $100,000 to over a billion currently, and we essentially invest in late-stage venture-backed growth-oriented companies that are typically doing hundreds of millions or billions in revenue.

These companies historically would have already been public, but based on various market dynamics that I won't bore you with, these companies have just stayed private for longer and longer and longer. And so your average retail investor who is only exposed primarily to the public market misses out on a lot of this private market growth that's happening, and so we try to solve for that through the interval fund structure.

I'm sure we'll hit on themes during a bit, but we think it couldn't be a better time to be allocating capital to this asset class. If you're looking to exit, not a good time. These are long-term strategies, and if you don't have multiple years they're not for you. And so we can talk about themes, about valuation, and capital raisings, and exits I'm sure during the panel, but I'll pause there for now.

Michael Grayson: I'm Michael Grayson, I'm with First Trust Capital. First Trust Capital is First Trust Portfolios alternative investment division, and so the legacy of that business has always been private partnership investing for the 3(c)(7) qualified purchaser clients. We also manage daily liquid products as well, so ETFs and mutual funds in the alternatives arena. And where we've been seeing a lot of appetite from our advisory clients today is in the interval fund space, we think it's a really nice structure.

As you think about those three product development buckets, I lay it out being mutual funds and ETFs on the liquid alternative side, then moving down the accreditation and liquidity spectrum to QP-only, less liquid private partnership investing and private equity, real estate, private credit, direct co-investments. And then in between those two different structures sits the interval fund, which we think is a great vehicle for bridging the accessibility gap for a lot of clients who can't access private partnership investing, and as portfolio managers having the flexibility to own some of those true alternative assets that you can't hold in a daily liquid vehicle like a mutual fund or an ETF. And so we have come to market with three interval funds as of late. Our first one was incepted in 2017, and then we've launched two more products this year that I'm happy to discuss on the panel today.

Kevin Dockrell: Kevin Dockrell, institutional portfolio manager for BlueBay Asset Management. So for those of you not familiar with BlueBay, we are headquartered in London but with investment offices in Stanford, Connecticut and Minneapolis, Minnesota. Run about $100 billion across all areas of fixed income, but we're really focused on alternative credits both public and private.

Within that $100 billion figure we run about $15 billion in global leverage finance, and within that we run an interval fund in partnership with our partners Destra Capital, which would be the focus of much of my comments today. That interval fund is called the International Event-Driven Credit Fund, effectively stressed, distressed, special situations across the global landscape. So that'll be the main focus of my comments as we speak.

Milwood Hobbs, Jr.: Thank you. Good afternoon, I'm Milwood Hobbs, Jr. I'm head of originations and co-lead our direct lending strategy at Oaktree Capital. For those who don't know Oaktree, we were founded in 1995 by Howard Marks and Bruce Karsh, we've been credit investors since then. We manage about $160 billion in private funds, we've got a public BDC, OCSL, and we've also got private BDC capital.

I think our hallmark is we price risk, and over the last few years we haven't really priced risk, and we're now in a market where you can price risk. And so with the banks and with Dodd-Frank, private capital, private credit as you know has grown to be a pretty big asset class. And so look forward to giving you my thoughts on that market.

Aaron Filbeck: Well, Milwood, why don't we stick with you just since you have the mic.

Milwood Hobbs, Jr.: I have the mic. But I don't have his accent.

Aaron Filbeck: I think maybe starting with credit, since we have the two credit people right next to each other. Milwood, let's start with you, just thinking about fixed income's finally interesting again for a lot of investors. And private credit in particular, a lot of floating-rate structures that are out there, floating rate is great until it's not.

Milwood Hobbs, Jr.: Right.

Aaron Filbeck: So maybe just give your thoughts on some of the deals that you're seeing and the impact of the rising rates on those places.

Milwood Hobbs, Jr.: So a little bit of a history lesson. If you remember in 2007, LIBOR, which was the benchmark, was at 5%, and most of the LBOs done in 2007 were LIBOR plus 200-250. I only know that because I was at Deutsche Bank and Goldman Sachs and did Nuveen, Ceridian, First Data, US Foods, and a host of other LBOs. So when the market corrected, the Fed policy was to lower interest rates. And so what you had was a positive effect on cash flows in

businesses because the spread to LIBOR was small, and as LIBOR declined, interest coverage ratios actually went up.

In this market, since we've had a benign interest rate market for the last I don't know how many years now, the spread to what is now SOFR has been higher. So most deals in private credit were SOFR plus 500 to 750, and we actually had floors because LIBOR was so low we had a 1% floor in those deals. SOFR's at 4.25%, so the interest rate on a first-lien deal is 10% cash pay. So in this market as we've experienced a decline if you will in the markets, interest rates and interest expense has actually gone up and cash flow coverage has gone down. So I think what that phenomenon will do is it puts pressures on companies to generate cash flow to pay interest obligations, number one. Number two, credit ratings, and if you will the rating agencies, will likely react to that, and so you can see downward pressure on ratings.

And I think just more broadly in the market, the public markets have repriced risk faster than private markets, there's still a lot of capital in private credit. And with the recent hung LBO situations, you are now seeing private credit actually step back a little bit. And so if you think about where deals are today, two years ago a tech LBO would price at SOFR plus 600, and today NASDAQ's down 30%, so your quote/unquote "LTV" is 42% just based on the movement in the markets, and then that spread that's 550 to 600 is now 750. And so between the moving rates and the degradation in equity value, you potentially could see a mark adjustment of 10 plus points on the loan, which you're not quite seeing that flow through BDCs and private assets.

Aaron Filbeck: Maybe you could pass to the guy with the accent.

Milwood Hobbs, Jr.: That was a lot.

Aaron Filbeck: Kevin, how about you in terms of I guess maybe views relative to Milwood's? But also just looking internationally since you have a unique perspective of being London-based.

Kevin Dockrell: Yeah, definitely we share some of the concerns in terms of credit quality. I think suffice to say, one of the bloody understatements of the century, 2022's been a very challenging environment for investors both on the equity side and the fixed-income side. Just given all of the crosscurrents that we face, be it inflation, be it geopolitics, be it the elephant in the room, China, be it you name it, supply chain disruptions, et cetera, et cetera. And it definitely feels, notwithstanding the uptick in sentiment and the rally that we've seen over the last week or so just on the back of the lower than expected inflation print, it still feels like we're on fairly shaky footing. And that feels more like a dead cat bounce or a bear market rally than anything that's going to lead us to be more constructive in our outlook.

So it all feels a bit doom and gloom at the moment from a credit perspective, but I guess from our perspective it's an actually pretty good environment given we're focusing more on the stressed and distressed segment of the market. We just think that it's a very, very good opportunity set to really look to pick up mispriced or misvalued securities. So we think it's

actually quite a good environment if we're sifting through the rubble what has been a fairly bad environment for credit.

Aaron Filbeck: Thanks. Christian, maybe we can move over to equities real quick. You alluded to some of the themes within the equity market, and specifically within venture and growth. Maybe let's start with valuations and where those have come, especially since we've seen public markets sell off so much. What spillover effects have you noticed in the venture and growth area?

Christian Munafo: Yeah, so if you look at what the public market considers to be high growth in the software space which the public market deems typically north of 20%, that's low growth in our world, but you're kind of high-growth software oriented enterprise grade businesses are currently trading somewhere around nine times revenue, pre-Covid that was around 13 times. And if you factor in Covid, over a five-year lookback you're looking at closer to 20 times. So we've definitely pulled back and re-rated in those high-growth oriented positions, and that has trickled into and will continue trickling into across all markets.

But it's not easy to paint the whole ecosystem with a broad brush, it's more of a bifurcation from our experience doing this for a couple decades. Your better best-in-class, differentiated, sustainable businesses with strong operating metrics, good syndicates, large TAMs, et cetera, good management teams, those companies have and will continue raising capital at reasonable valuations. It's the companies that are less differentiated that have weaker balance sheets, higher burn rates, they're not yet profitable or they have no path of profitability, weak syndicates.

Those are the companies that are most at risk for either egregious terms on new rounds getting bought on the cheap or going away. We think a lot of them are going to go away, and a lot of them frankly should go away. Capital's been too easy over the past decade let alone few years, and a lot of these what we would call "copycat companies" just don't really deserve to be around. So we'll see a correction for sure in that landscape. But you can't paint the entire ecosystem with a broad brush.

So that's kind of how we view valuation, and that leads into capital raising. So similarly, your better companies as we said are going to be okay from a capital raising perspective. They may not raise capital at the multiples we saw over the past few years, which were not sustainable, but most of the companies that need to raise capital that are in that class are not having a problem doing so. Again, it's that lower class of companies that are less differentiated that have more problems. And if you're a company that needs to exit, this is not the environment. We don't even think 2023 for the most part will be in an attractive environment for these types of companies to exit.

Now that creates also a massive supply side opportunity, because investors and shareholders in these companies that never imagined them being private for 10, 15, 20 years, increasingly want some liquidity. And so in the market, groups like us can take advantage of that by providing a secondary source of liquidity to players in this ecosystem, as well as financing these companies through new rounds with much more investor-favorable terms. So it's not all doom and gloom,

but there absolutely is some gloom that I think the most sophisticated investors will always take advantage of.

Aaron Filbeck: Are you finding good quality companies that aren't struggling in this environment, are they just not raising capital because they don't need it? And there's a fear that you can strike a new valuation and it might not be justified?

Christian Munafo: Well, the better companies raised capital before we even came in to 2022. A lot of these folks have been around for a while, and so if we look at our portfolio, 85% of our portfolio raised capital before in the last 12 months leading up to this year and a lot of our companies are already profitable. So I think the companies that were prudent were already raised.

You are seeing companies raise up rounds, you're seeing companies do down rounds, and you're seeing a lot of companies that are just basically pushing and saying, "We're going to raise at a flat round." So they say, "We've grown 100% since our last round," the market says, "Well, we've re-rated 50%." So net-net, a lot of these groups are basically saying, "Let's call it a push. We'll do a convertible instrument that we'll price at a future date, maybe 12-18 months from now." So again, it's segmented across the asset class.

Aaron Filbeck: Great. Mike, you have a unique perspective just given the multi-asset approach that you all take. How are you thinking about asset allocation and allocating across the multiple vehicles that are available to you?

Michael Grayson: Yeah, absolutely. There's really, as we're thinking about being able to provide different types of advisory solutions through an interval fund wrapper, a lot of the funds that we see in the marketplace that have been able to generate alpha do have a more narrow sector-specific focus. And so when we're thinking qualitatively about how we break down the private limited partnership alternative investment space, it's really into different asset class sectors, private and growth equity, private real estate, private credit, hedge fund strategies, as well as co-investments.

So one of the reasons why we as PMs like the interval fund structure a lot is because a lot of those asset types, or most of those asset types fit the interval fund wrapper very well, and so it's a great asset allocation tool for advisors who don't want to build fund-by-fund allocations. Candidly away from the strategy side, the structure has nuances from a liquidity standpoint. There are ticket charges associated when you're sitting in an advisor's seat. A lot of times there are non-standard asset potentially custody fees with alternative investments.

And so for us, if we can take all of these alternative asset class buckets, package them into one interval fund solution without creating an asset-to-liability mismatch for any of the assets that we own relative to the interval fund structure liquidity schedule, we think that's kind of a great single ticket solution for an advisory client that has their equity allocation, they have their fixed

income allocation, and they're thinking how do I scalably build a true alternatives third leg of the stool for your typical retail asset allocation-oriented client?

And so this was our first foray into interval funds where we effectively took a multi-asset approach, tried to own a best ideas portfolio of what we think are really interesting private and growth equity investments, real estate investments, private credit, hedge fund strategies as well as some direct co-investment opportunities, and then package them into a more client-friendly vehicle which is the interval fund. And so that's in a nutshell why we like the interval fund structure so much as a research team, it really provides us the flexibility to own a wide array of differentiated and unique alternative asset classes.

Aaron Filbeck: So you mentioned co-investments. How are you thinking about co-investing right now? Do you do secondaries as well?

Michael Grayson: Not a lot in the secondary space. The legacy of our business is private partnership investing, and a lot of it is from an arm's length LP standpoint. But when we work with a general partner, again I keep walking through these different sectors, but we try and have access to managers within each of those buckets of equity, credit, so on and so forth. As an LP you have to ability right now in this capital raising environment to really negotiate and leverage your capital to get access to co-investments that reduce economics with a lot of the GPs.

And for us when we're building a multi-asset portfolio in an interval fund, the shortcoming is we're trying to avoid a fund of funds concept that has high underlying acquired fund fees and expenses. And so one of the ways we can sidestep effectively the traditional fees associated with alternatives is by doing direct co-investments, alongside our managers piggybacking effectively off commitments we've made on our private partnership business and doing direct deals at reduced or zero economics.

And so when we get that deal flow on our private partnership business, we effectively use our interval fund solutions to piggyback off that deal flow and take advantage and capitalize on co-investment opportunities. So I certainly think, especially from an asset allocation perspective, co-investments are going to be a direction that a lot of portfolio management teams end up going when constructing interval fund portfolios.

Aaron Filbeck: Kevin, maybe starting with you, and then Milwood as well on the credit side again, distressed, this is obviously probably a really good environment for finding distressed opportunities. What are you seeing in the distressed market? Whoever wants to go first, but you've got the mic.

Milwood Hobbs, Jr.: So interesting enough, the market with the hung bank situation, you can buy first-lien risk or originate first-lien risk at SOFR plus 750, which is roughly 12% and the OID's 97. And by the way, with a BDC or a lot of the funds, you can actually get leverage on that, so you can achieve mid-teen returns being senior in the capital structure.

So when you think about distressed, the problem, and you're starting to see chinks in the armor, companies are starting to have some issues. The challenge becomes do you really want to play lower in the capital structure in a market where valuations are probably going lower? Legacy deals that were done over the last three or four years are starting to have non-accruals, there's some non-accruals out there. And I think for us we're being patient and we're more picking either a sector or a theme for what we view as distressed or stressed opportunities versus just saying, "We're in a distressed environment."

And so I think you have to be careful when you're looking at companies that are experiencing stress, because in the new issue I can get to a 15% being top of the capital structure. And that just feels more interesting right now than trying to get an 18%, being lower in the cap structure subject to a valuation degradation.

Aaron Filbeck: Kevin, anything thoughts from you?

Kevin Dockrell: Yeah, definitely agree to be honest. And in terms of the strategy or the fund that we're offering, we're not really trying to shoot the lights out either, we're looking to get to maybe a 10% net return target over a cycle. And if you look again illiquid public markets, high yield, pretty not far off that in terms of all-in yield almost at a nine handle.

So again, to echo Milwood's comments as well, you don't really need to go reaching to get to that mid-teen target. So I think from our perspective, it's just we're seeing lots of, like if I look at a desk managing this fund, they're just seeing so much more opportunities than they have at any point since they've been managing it. So it's a really pretty good environment I'd say for a flexible, nimble strategy that's focusing on these segments of the market.

Aaron Filbeck: So are you mostly looking in the public markets at this point versus direct origination?

Kevin Dockrell: It's a good question. So we're pretty agnostic, but I think the key about the fund is flexibility. We have the ability to go into public, we have the ability to go into private. We almost think of it, we want to be more illiquid or liquid and we're agnostic between bonds and loans, we don't really have a sector bias or sector theme. So I think the tagline is, "When visibility is low, flexibility needs to be high." So we really are just maintaining that, we just go where the opportunity set is. And for choice at the moment it's in Europe over US, and it's really just more idiosyncratic bottom-up driven as opposed to any sort of sector thematics.

Milwood Hobbs, Jr.: So on the public versus private, what we've tried to do is if we think there's an interesting public security out there, we've tried to then reach out to that sponsor and create a private tranche adjacent to that public security where we control it. The problem with public debt is in a tranche that has 50 investors, no one has the same agenda. And so with a public mark, if one portfolio manager decides they don't want to be in that position, they actually

could drive the valuation lower on that position just because the liquidity's pretty bad. So we'd rather control our own destiny and do a side-by-side tranche that's private and just us.

The other thing you have to think about with the public markets is that you don't really have control of the [inaudible], and so when we think about public deals we think about large sponsors, large EBITDA, good businesses, versus just anything out there in the public markets.

Aaron Filbeck: Maybe sticking with you, and we've talked a little bit about the structure, I know mostly Mike has talked through that. But Milwood, I know you're mostly focused on deal origination and the deals themselves, but I guess when you look at Oaktree you've got a lot of different vehicles that you can manage a portfolio in. What are some of the things that you'd change or maybe potentially give up, or maybe are an added benefit to the different structures that you offer these strategies in?

Milwood Hobbs, Jr.: Sure. I think what, and this is one thing that a lot of our competitors don't focus on, is the leverage in the fund. So a BDC can lever up to two times, we will oscillate. And if you look back at 2020, we were not that levered because we felt like the market opportunities, we could get the returns without leverage driving the return. And so these leverage facilities are issued by banks, the banks are hemorrhaging on hung LBO debt.

The next phase of that is, "Oh wait, so I'm hung on debt that private credit is going to buy, and I'm levering that very same debt though the private credit fund." And so you have to be careful around the leverage of the BDCs and some of these private closed-end funds because leverage exacerbates issues. And so what we try to do is we manage to make sure we can price the risk, we don't look at leverage as a driver of returns. And I think that's one thing you have to keep in mind with some of these strategies.

So leverage is one strategy, the other thing is that we cross-pollinate. So in a lot of our deals and because of my group, every deal that comes in Oaktree now, more than one strategy sees it. So we idea share and we cross-pollinate, and so there could be a deal that's in the BDC that's in four different strategies within Oaktree. And so you've got that breadth where it's not like the BDC is taking a position that the rest of Oaktree doesn't have on its books too, we tend to cross-pollinate and share the risk. And if it's good for the BDC, generally it's good for other sleeves within Oaktree not just the BDC.

Aaron Filbeck: Christian, I'd be curious to your thoughts on this jut given late-stage venture private equity, you don't necessarily have those cash flows that are constantly kicking off like you might have in private credit. So how do you manage your strategy in a semi-liquid wrapper knowing that there might be redemptions and retail investors that are moving in and out of the structure?

Christian Munafo: Yeah, and just to clarify, the asset class that we invest in doesn't really have leverage, these companies don't deserve leverage. If you're not printing cash, you don't deserve to be levered. So when we look at the capital structure of venture-backed companies, even ones

doing hundreds and millions and billions of dollars, you'll rarely ever see any meaningful debt on the balance sheets of these companies.

So that's one aspect of their capital structure that you don't have to really worry about. And the funds also don't typically use leverage. If they do, they shouldn't be employed. That's not a really prudent thing to do. So leverage has definitely been overutilized we think across the entire asset class. I've seen my colleagues in the buyout space using it way too freely, and we know how that story typically ends.

So with regards to how do we manage liquidity in a strategy where we have all illiquid assets? Well, there's obviously certain measures that you're required to abide by as a 40 Act fund, so you need to maintain certain levels of liquidity in the fund at any given time. We have a redemption line of credit which we can use, which we don't really tap but we have as a backstop. We have inflows, so our inflows are three to four times what the quarterly outflows tend to be.

So as long as you're bringing in capital, and the only reason you do that is if you're doing a good job for your clients. Then again, you don't deserve to be managing a fund if you're not doing that. But so you have inflows, that'll come in, that'll offset your quarterly redemptions. Which as many of you know are typically 5% of the net assets of the fund on a quarterly basis. And then you have excess cash reserves for offensive and defense in terms of your overall portfolio construction.

In a normal environment, we'll also have companies that are exiting, that are getting acquired or going public. None of that's happening right now because the markets are just awful. And then we may opportunistically sell private positions into the private market. So we're not doing that now because the valuations are not attractive, but in the past few years we've sold a number of positions to other private market investors.

So if we've hit our underwriting case of two, three, four times, we're happy to take our chips off the table or at least lock in some type of a return and then ride the rest as house money. So we've been around for nearly a decade, the fund has never been as large as it is now and we've never had an issue, but it does require active management. You have to be very thoughtful about maintaining proper liquidity.

Aaron Filbeck: Great. I want to finish up with Mike and Kevin, but also if any of you have questions you want to ask the panel, we've got about 10 minutes left so feel free to raise your hand or whatever, run up on stage.

Mike, so you've got an interesting mix here where you're managing multi-asset portfolios so there may be some cash flow kickoff that occurs. But you've also got LPs, co-investments, very different liquidity profiles within a semi-liquid fund. So how do you manage knowing that you've got this fund structure that may require some redemptions periodically.

Michael Grayson: Absolutely. I think just doing, to Christian's comments, the best you can from a portfolio management perspective to try and really align the underlying portfolio with the

fund's liquidity first and foremost is how we think about it. In terms of the 5% liquidity that's provided quarterly to investors, trying to have sufficient coverage of that redemption rate where we're typically running liquidity sleeves in the neighborhood of 15-20% in our interval fund solutions. Knowing that again, if you give retail investors the option to redeem on a quarterly basis, there are going to be redemptions each quarter in a benign market, certainly in a stressed market, and so you need to have access to daily liquid strategies in your portfolio to be able to provide that liquidity.

Each quarter we typically run, as I mentioned, a liquidity bucket of about 15-20% to actually conservatively try and run a full year's worth of liquidity. Because 5% per quarter times four quarter, you need 20% liquidity per year in our interval fund solutions, and we think that's a really good kind of first-line of defense to meet those investor redemptions each quarter. From there obviously, the benefit of the structure is that it's semi-liquid or relatively illiquid, so trying to capture illiquidity premiums and yield premiums in the rest of the portfolio.

Aaron Filbeck: Maybe finishing up with you. Any other additional thoughts you'd add?

Kevin Dockrell: Yeah, to be honest, the interval fund structure is absolutely perfect for the strategy that we're running, I'd say. I guess from the end client's perspective it gives them access to a skill set or a strategy type that they may not be able to access elsewhere, and from the portfolio management perspective it's great because there's no mismatch between the liquidity or the time horizon between the assets that we're purchasing and the liquidity terms that we offer.

If I think about, not to go into the detail on the fund itself, but we have four different sleeves, the first of which would be what we would class as core income, your on-the-run liquid bonds and loans which we can sell very easily to meet redemptions. We also have, as I said, event-driven credit and then restructurings and we also have a short bucket. So if you think about each of those four buckets, we'll be more or less compelling at different points in the cycle. But if I think about the quarterly liquidity profile, touch wood, in the four years we've been managing this there's been absolutely no issues in terms of giving clients that liquidity as well.

Aaron Filbeck: Any questions from the audience? Yeah, go ahead.

Audience: As an advisor thinking of putting money into this space, my biggest concern is the quality of the net asset values that get quoted. On occasion I'm dubious, shall we say. If you could talk about how you price and value the assets in your portfolio, I'd be interested in hearing what you have to say.

Kevin Dockrell: Milwood laughed, so I'm going to pass the mic to him.

Milwood Hobbs, Jr.: Oh, I'm baffled by it too. So finance is art and science, right? The science is interest coverage, the calculation of EBITDA. The art part of is what's your assumption on add-backs, what's your weighted average cost of capital, what's the free cash flow? And so

quarterly there's two components to the mark, there is the yield component that's just based on moving rates, that's pretty scientific. The other component is a DCF or some sort of enterprise valuation that the Duff & Phelps, the Houlihan's, the Lincolns, they evaluate your position based on those metrics, and that's a bit of an art.

And so the problem with the mark is, generally speaking if you can weave an intelligent story around why you think a business despite everything that's going on should be marked where they think it should be marked, you can manage that a little bit. And I think that's why you should have the concern. Where if you looked at one security, it likely has a different mark with everybody who's in that security in the BDC space. So I think the way we think about it is we look at marks as where can we sell the risk?

The other thing we do is if we're going to do an add-on, what I tell clients is the add-on is not necessarily driven by just the risk, but if I priced it originally at SOFR plus 697, but it's marked at 94, I'm not going to do an add-on at SOFR plus 697 because I'm immediately going to recognize a loss to 94. And so just conceptually the way we think about pricing new risk is somewhat driven by where that risk should be priced in the current market. And I think that element is missing from some folks' thinking about it in the context of the current market.

Aaron Filbeck: Any other thoughts because I take other questions?

Christian Munafo: Yeah, we have an interesting framework that we have to use. So when we went to the SEC about a decade ago and said, "We want to launch this venture growth fund for retail," they said, "Great." By the way they didn't say great, they would never say great, but let's play along with me. So, "Great, you're going to level the playing field to allow retail investors to get access to all of this private market innovation that's happening before they go public. And arguably at a point where there's not much value left to harness for quite a period of time. But if you're going to offer it daily, you have to manufacture volatility."

So what that essentially meant was working for them almost a year, and third-party valuation firms and auditors to basically come up with a more dynamic valuation framework than what a traditional private market fund will do. So if you have GP-LP funds in your portfolio, those of you that are familiar with them, obviously I think the panel is up here, and I manage those funds historically, those will typically be valued quarterly. And most often than not the main driver of valuation will be the last private round valuation that the company raised capital at.

We don't have the luxury of doing that, because if that happened two years ago that's a stale input, that's not going to work with a framework like ours. So that becomes A input, a static input, as well as 409A option pricing [inaudible] options, those are static inputs. But those don't mean a whole lot when you have an environment that's changing every day with a fund that prices every day. So we have to also have a slew of more dynamic inputs including tracking public comps, tracking public funds who also own pre-IPO companies. If there's secondary trading activity, looking at those feeds. If there's exit comps, inputting tose multiples. So you essentially have an elaborate framework that is quite comprehensive.

None of these valuations, to Milwood's point, are perfect. This is a lot of art here. But having managed both funds, I think the daily valuation that you have with the valuation framework that incorporates both static and dynamic inputs, provides you with a much more accurate assessment of what the true current fair market value is.

And the last point I'll make is, for those of you that have private equity funds, and you have capital accounts in those funds, up until probably September the most recent capital account statement you had was March 31st because your June 30th statement didn't probably get published until maybe August, September. A lot's changed in the world since March 31st. So folks say, "Oh, my private equity portfolio's doing great." Is it? You have a stale input. We don't have the luxury with an interval fund that prices daily of doing that. And so that historical lag effect that you hear the market talk about between public and private markets is often driven by what I just talked about, quarterly pricing and then publishing 60 to 90 days after the quarter. Interval funds, if they're managed correctly, don't have the ability to do that.

Milwood Hobbs, Jr.: Now I'm going to say the complete opposite of what I said earlier. So in public securities, the mark doesn't necessarily represent the credit risk of that company, that mark represents inherent liquidity or lack of liquidity generally in that. Because with two third, three quarters of the loan market is cov light. So companies don't really go from par to 90, generally that's a liquidity mark, they'll go from par to 60 with a credit mark. And so we sometimes look at that as an ARB in the public markets and we might say, "Wow, that credit is actually better than the mark," and we may buy that company because the marks really only reflecting liquidity versus true credit risk.

Aaron Filbeck: Well, we are out of time. I'm sure you guys will be around afterwards, I know we had a couple other hands raised. Bu please join me in thanking our panelists.

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