BREAKING NEWS
28 May 2026

Getting Ahead of the Curve – Identifying Stress Before it arrives

Private credit fundamentals remain healthy, as defaults and non-accruals remain low. On the surface, that is a reassuring picture, but these metrics are lagging indicators and only tell you where credit health has been. By the time they spike, the stress has already arrived. So where should investors be looking instead?

Recent headlines have focused on a modest uptick in non-accruals, driven by high-profile upper middle market names like Medallia and Affordable Care. While this trend bears watching, we view this as a normalization from historically low levels, and not a sign of broader deterioration. That said, the important question is what comes next. For that, you need to be watching the right signals.

We focus on three leading indicators that tend to flash warning signs well ahead of a credit cycle turn: amended PIK or "bad PIK" usage, loans marked below 80 cents on the dollar, and interest coverage ratios below 1x. Today, each of these metrics has either improved or held steady relative to recent quarters — pointing to a stable environment rather than one of stress. Combine that with a still-supportive macro backdrop, middle market borrowers appear well-positioned to navigate the current environment.

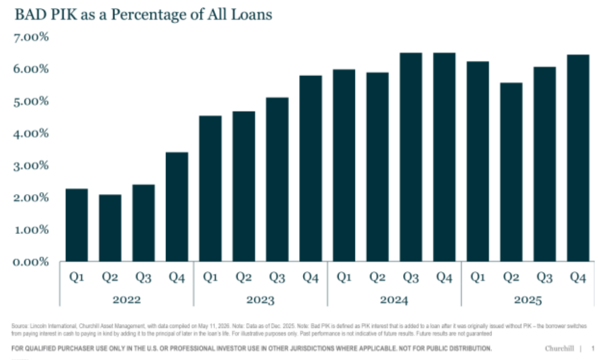
WHAT'S LEADING

- We believe there are three indicators that investors should watch to determine if stress is building in the loan book, or the private credit asset class more broadly speaking.
- Based on the indicators we are tracking, stress appears to be contained. However, interest coverage ratios below 1x bear close watching, particularly if the Fed keeps rates at current levels for the rest of the year – shifting back to "higher for longer" environment.

PERCENTAGE OF PIK THAT IS AMENDED – "BAD" PIK

- Payment-in-Kind, or PIK, has become a major focal point for investors in recent years. But not all PIK is created equal.
- PIK structured at origination is generally viewed as a deliberate feature of the deal — whether used to support company growth, preserve cash flow flexibility, or help win a competitive deal — and is not inherently a signal of stress. It is PIK that is amended – where a borrower switches from cash interest payments to accrued interest – that signals potential stress. We call this "Bad PIK."
- "Bad PIK" has risen in recent years but has stabilized at 58% of all PIK loans – down from a peak of 62% in Q4 2024.[1]
- To put this in context, only 11% of all loans carry any PIK at all – meaning "Bad PIK" represents just 6.4% of the total loan universe (see Exhibit 1).[2]
- **Churchill Take:** The stabilization in "Bad PIK" over recent quarters is an encouraging sign. Given that the rise in "Bad PIK" can be viewed as a shadow default rate, this shows that credit conditions have been stable rather than deteriorating. We are encouraged that "Bad PIK" has pulled back from its Q4 2024 peak — though we will continue to monitor this closely. If the Fed remains more hawkish than markets currently expect, borrowers with already strained cash flows could come under additional pressure.

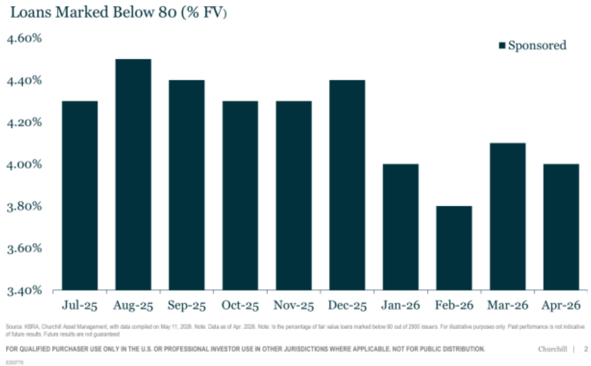
Exhibit 1: Bad PIK Levels have started to stabilize



PERCENT OF PORTFOLIO MARKED AT 80 OR BELOW

- Loans marked below 80 on a cost basis indicate signs of stress as they are typically treated as non-performing.[3]
- At just 4% of the total KBRA universe, loans marked below 80 remain low and have been largely unchanged over the past year (see Exhibit 2).[4]
- However, given these loans are not traded, there are some that think the barometer for impairment is higher. Even looking at loans marked below 90, we have not seen a meaningful change over the last few months – reinforcing that stress does not seem to be broadly building.
- **Churchill Take:** The decline in loans marked below 80 is an encouraging signal that credit conditions have stabilized and, in some cases, modestly improved. Even the percentage of loans marked below 90 has been stable, indicating no deterioration in credit quality. While pockets of stress exist in areas like Software, marks are not moving in a direction that signals broader concern.

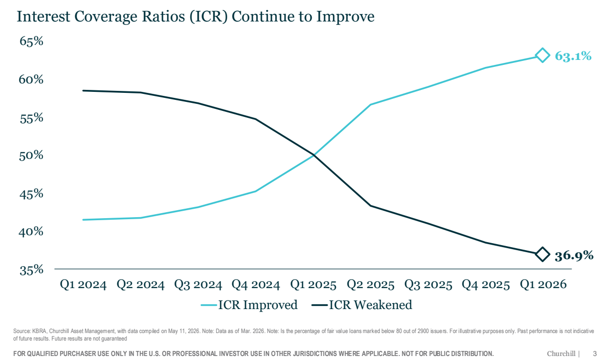
Exhibit 2: There has been an improvement in loans marked below 80



PERCENTAGE OF THE PORTFOLIO WITH AN INTEREST COVERAGE LESS THAN 1X

- The interest coverage ratio measures a borrower's ability to meet its interest obligations relative to its earnings. A ratio below 1x means earnings are no longer sufficient to cover the interest bill – a threshold that has historically been a reliable sign of stress.
- According to KBRA, 25% of middle market borrowers currently carry an interest coverage ratio below 1x.[5] However, the more telling figure is that only 4% of borrowers are actively seeing their coverage ratios decline – suggesting the problem, while present, is not broadly spreading.[6]
- Concentration also matters here. The stress is not evenly distributed across the portfolio, as it is disproportionately concentrated in Software and Consumer Retail names.[7]
- The broader picture is more encouraging. Nearly 65% of companies in the KBRA universe are seeing improving interest coverage ratios, which has pushed the median up to 1.6x from 1.5x the prior quarter (See Exhibit 3).[8]
- The primary risk to this improving trend is the policy rate environment. Markets are currently pricing in approximately half a rate cut for 2026, suggesting we may remain in a higher-for-longer environment.[9]
- **Churchill Take:** The direction of travel is encouraging, but the destination is not guaranteed. While a majority of borrowers are seeing coverage ratios improve, those already below 1x have little cushion. With markets pricing in no further rate relief in 2026, this will be a key factor in whether this trend holds.

Exhibit 3: Interest Coverage Ratios have improved since the Fed started cutting



BOTTOM LINE

- Pockets of stress exist — concentrated in certain upper middle market names and sectors like Software and Consumer Retail — but the data does not support a narrative of broad-based deterioration. Across the three leading indicators we track, the picture is one of normalization rather than a credit cycle turn. **While we are closely watching how interest coverage ratios evolve in a high-for-longer rate backdrop, we do not believe today's environment is flashing red.**

ABOUT CHURCHILL ASSET MANAGEMENT

- Churchill, an investment-specialist affiliate of Nuveen (the asset manager of TIAA), provides customized financing solutions to U.S. middle market private equity firms and their portfolio companies across the capital structure. With over $64+ billion of committed capital under management, we provide first lien, unitranche, second lien and mezzanine debt, in addition to equity co-investments, secondary solutions and private equity fund commitments. Churchill has a long history of disciplined investing across multiple economic cycles and our unique origination strategy and investment approach are driven by nearly 200+ professionals in New York, Charlotte, Chicago and Los Angeles.

For more information, please visit us at nuveen.com.

1. Lincoln International, as of Dec. 31, 2025.
2. Lincoln International, as of Dec. 31, 2025.
3. MSCI, as of Sep. 17, 2024.
4. KBRA, as of Apr. 30, 2026.
5. KBRA, as of Apr. 30, 2026.
6. KBRA, as of Apr. 30, 2026.
7. KBRA, as of Apr. 30, 2026.
8. KBRA, as of Apr. 30, 2026.
9. Bloomberg, as of May 21, 2026.