

Business of Private Credit: Rain or Shine

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Experienced private credit managers build all-weather playbooks designed to make it through any business cycle or headline risk. It's critical for having a successful track record of low defaults and losses because middle market loans don't trade the way broadly syndicated loans or high-yield bonds do. Even with resilient companies in defensive industries, once you book it, you own it.

So, what happens when one of these ground-level deals runs into trouble? Less-cyclical sectors give you more time to react, but stuff still happens. And as we'll discuss in later episodes, private equity ownership provides helpful oversight and professional management, but the higher leverage in buyout financings leaves less room for mistakes.

HVAC, fire and security systems, commercial landscapers, and wastewater management are good examples of "old economy" core middle market businesses. They are essential, must-have services with recurring revenues, sticky customers, and strong free cash flows. They also tend to be less driven by consumer sentiment. The best performers are sustained by having an intense focus on customer service, creating moats around their client (and vendor) relationships.

Yet these are still small-medium-sized enterprises, many of which are experiencing institutional ownership for the first time. Trouble comes in various guises, both internally and from many outside factors. Management overbuilds or overextends their M&A programs. Poor cash controls can create unexpected working capital shortfalls. A large customer unexpectedly walks. A key vendor misses a delivery. A top salesperson goes to a competitor. A storm wipes out a major facility.

Experienced lenders and their sponsor partners expect problems like these and create contingency plans. In businesses where cash goes out before it comes back in, structuring around the working capital cycle is essential. Underwriting customer durability focuses not just on concentration risk, but what keeps the customer from going to a competitor.

In regulated industries, supplier qualification processes create real switching costs that protect incumbency. When a business serves multiple end markets, those segments are less likely to stumble at the same time. Sponsors reinforce this work by bringing industry expertise via operating partners who coordinate with management teams on corporate development and strategy.

This discipline shows up in the numbers. As our [Chart of the Week](#) shows, defaults for service-oriented middle market companies run below those of cyclical peers and the BDC average.

Allocating toward defensive, service-oriented businesses isn't a retreat from return potential. It's a disciplined strategy built around what happens when things go wrong, because sometimes they do. Every portfolio has to weather storms. The good managers don't just hope for sunshine; they've already packed the umbrella. win, place or show. It just has to finish the race.