

Overlap in the Upper Middle Market: Why Diversification Becomes More Difficult

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- A surge of capital into the upper middle market has led many large private credit managers to compete for the same small pool of companies, increasing portfolio overlap across platforms.
- Syndicated structures and limited deal flow mean multiple managers often hold the same loans, reducing true diversification for advisors allocating across large providers.
- The core middle market offers a far broader, more fragmented opportunity set, allowing lenders to build portfolios with meaningfully less overlap and more differentiated exposure.

In 2024, 84% of all private credit capital raised flowed to mega-managers, many of whom compete for a relatively limited number of transactions in the upper middle market.¹ As a result, capital supply in that segment has increasingly outpaced opportunity, intensifying competition and compressing returns.

By contrast, the [core middle market](#) represents a significantly broader and less crowded investment universe. Beyond offering more attractive risk-adjusted returns, managers that focus on this segment gain access to a deeper pool of opportunities with greater potential for diversification.

Crowding and Convergence in the Upper Middle Market

The upper middle market encompasses a relatively small population of companies, which has created a highly competitive environment for lenders. In this segment, many financings take

¹ Pitchbook. 2024 Annual Global Private Debt Report.

the form of syndicated loans, with multiple managers participating in the same transaction. While this structure can provide diversification within a single fund, it often results in substantial overlap across managers and portfolios at the industry level.

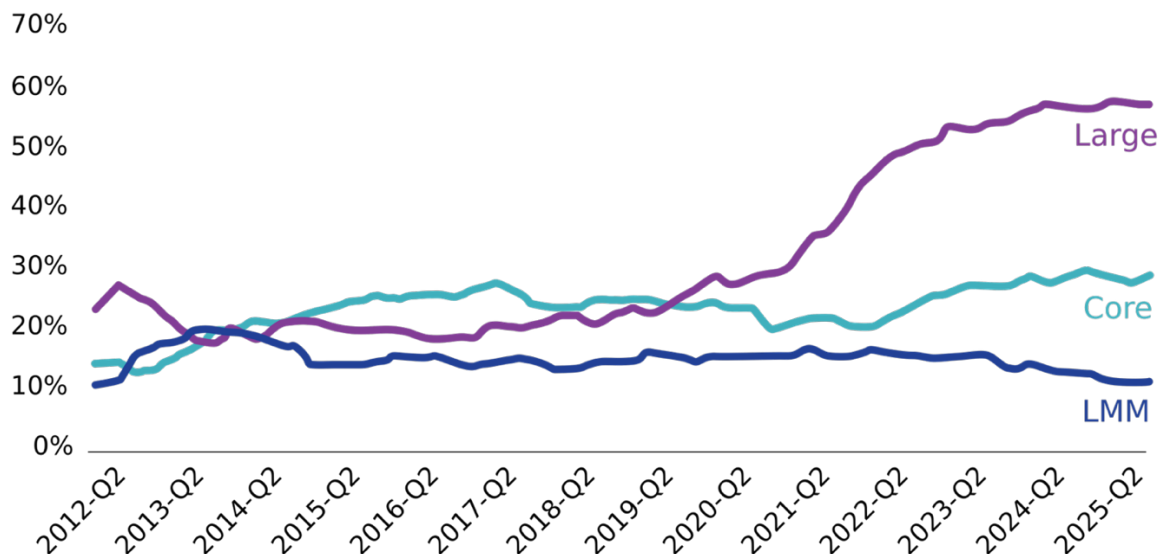
For advisors constructing private credit allocations across several large platforms, this dynamic can lead to portfolios that look more similar than expected. Separate managers may appear distinct at the surface level, yet ultimately hold exposure to many of the same underlying borrowers.

The competitive pressures in the upper middle market also limit lenders' ability to control deal terms. As a result, investors may face:

- Lower credit spreads
- Fewer financial covenants
- Compressed due diligence timelines

These factors can materially increase risk, particularly late in the credit cycle. Raymond James' research reinforces this point. Analysis of loan portfolios across business development companies (BDCs) has shown significantly higher portfolio overlap among large, upper middle market lenders compared to managers that focus on directly originated loans in the [core middle market](#).

Weighted Average Portfolio Overlap by Market²



² Company Filings and Raymond James Research



Diversification Considerations for Investors

For investors allocating capital across multiple large private credit platforms, portfolio overlap can create unintended concentration risk. Investing with two or more managers does not necessarily ensure diversification if each manager is operating in the same crowded segment of the market and participating in the same syndicated transactions.

This overlap is not a reflection of manager oversight or inefficiency. Rather, it is a structural outcome of a concentrated opportunity set and the widespread use of syndication in the upper middle market. The key takeaway for investors is that manager selection alone may not fully address diversification risk if exposure is concentrated in the same market segment.

The Advantage of the Core Middle Market

The broader middle market consists of nearly 200,000 companies, representing approximately one-third of the U.S. economy and generating an estimated \$10 trillion in annual revenue.³ Within this universe, the [core middle market](#) (companies with \$10 to \$50 million of annual earnings) remains meaningfully underserved by traditional lenders.

With less competition from banks and large asset managers, this segment offers:

- A larger and more diversified opportunity set
- Greater ability to negotiate lender-friendly terms
- Lower portfolio overlap across managers
- Enhanced potential for true diversification at the investor level

PennantPark's Core Middle Market Focus

Private credit opportunities vary widely by market segment, and not all areas of the market are created equal. Investors should carefully consider how capital concentration and competitive dynamics may affect portfolio outcomes, particularly in saturated segments such as the upper middle market.

PennantPark has focused on the [core middle market](#) for nearly two decades, navigating multiple credit cycles including the Global Financial Crisis, the post-2010 expansion, and the COVID-19 downturn. Throughout these periods, our disciplined, relationship-driven approach has remained consistent, supporting a resilient and durable lending platform.

We welcome a conversation; please contact invest@pennantpark.com or the professionals listed below.

³ National Center For the Middle Market, 4Q 2023 Middle Market Indicator Report



About PennantPark:

PennantPark was founded in 2007 as an independent middle market credit platform. The firm was founded by Art Penn, a private credit industry veteran that previously co-founded Apollo Investment Management. We have invested over \$26 billion across multiple economic and credit cycles since inception, and we manage \$10 billion in AUM⁴ today. PennantPark serves a broad range of sophisticated investors with product offerings that include business development companies, private capital funds, joint ventures, and other specialized funds.

Our highly experienced team primarily invests in the core middle market, targeting companies with earnings of \$10 million to \$50 million. These mid-sized companies are often overlooked by banks and large investment managers, resulting in senior secured loans that generally feature higher yields, lower leverage, and stronger lender protections when compared to the upper middle market and broadly syndicated loans. We focus on five key industry verticals where our track record is excellent and where we have the most expertise and experience. These industries include healthcare, government services, business services, consumer, and software & technology.

⁴ Assets under management ("AUM") is defined as the sum of gross asset values, unfunded commitments, joint ventures and undrawn available leverage for active funds as of 12/31/2024. Invested capital represents the cumulative sum of capital invested across the PennantPark platform since inception through 12/31/2024. Figures are rounded to the nearest billion.

PennantPark Contacts:



Scott McCabe

Managing Director, Head of Private Wealth Solutions

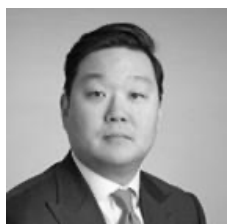
mccabe@pennantpark.com



Tyler Anthony

Senior Vice President, Private Wealth Solutions

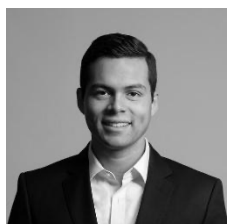
anthony@pennantpark.com



Brian Lee

Senior Vice President, Private Wealth Solutions

blee@pennantpark.com



Juan Ledezma

Vice President, Private Wealth Solutions

ledezma@pennantpark.com



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