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Non-Traded Business Development Companies: Illiquid Assets, Valuation Discretion, and Flow-Performance Sensitivity

Kenechukwu Anadu and Johannes Wasner[1]

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Abstract

Perpetual-life non-traded Business Development Companies (NT-BDCs), a type of private credit vehicle, offer periodic liquidity while holding mostly illiquid loan portfolios. Following elevated redemption pressures since late 2025, we ask two interrelated questions. First, does the leverage-valuation relationship differ between non-traded and publicly traded BDCs? Second, to what degree do NT-BDC flows respond to past performance? Comparing the same loan held by different BDCs at the same time, we find that, on average, this leverage-valuation relationship is more positive for NT-BDCs than for publicly traded ones. Also, NT-BDC net flows are positively related with past performance, driven primarily by inflows. Our results inform policymakers, academics, and market participants examining leverage, valuation discretion, and liquidity transformation in private credit.

JEL Classification: G23, G28, M41

Keywords: Business Development Companies (BDCs); liquidity transformation; private credit; illiquid assets; Level 3 assets; valuation discretion; flow-performance sensitivity

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1. INTRODUCTION

Over the past several years, the net assets in perpetual-life non-traded Business Development Companies (NT-BDCs), a type of private credit vehicle, have grown significantly. Indeed, net assets in NT-BDCs are over $380 billion in 2026, up from less than $28 billion in 2018.[2] Beginning in the fall of 2025, unusually large redemption requests from NT-BDCs raised concerns about stresses in the private credit sector and potential financial stability ramifications (see, e.g., Wirz, 2026; Brush and Scigliuzzo, 2026).

In this paper, we conduct two complementary studies on BDCs. First, we investigate whether the leverage-valuation relationship differs between NT-BDCs and publicly traded BDCs.[3] All else equal, loan markdowns have a larger effect on net asset value (NAV) at more levered BDCs and move them closer to their regulatory leverage limits. (Dividend payments are restricted if a BDC breaches this limit.) This may create an incentive to delay markdowns, which could be stronger for NT-BDCs, whose investors purchase and redeem at NAV rather than at a market price. Second, we examine the degree to which NT-BDC investors' gross inflows (i.e., share issuance) and outflows (i.e., share repurchases, both fulfilled and requested) respond to past fund performance.

We focus on these questions because NT-BDCs have several structural features that—in certain combinations—can generate or amplify financial stability risks: valuation opacity, illiquid loan portfolios, leverage, and semi-liquid redemption structures (see, generally, Goldstein et al., 2017; Federal Reserve Board, 2026).

We show that, on average, for the same loan in the same quarter, higher leverage is associated with incrementally higher loan valuations for NT-BDCs relative to publicly traded

[2] This likely includes legacy finite-life NT-BDCs.
[3] Throughout this paper, we use "publicly traded BDCs" and "traded BDCs" interchangeably.

BDCs. (Our results are similar in magnitude when we further restrict our sample to the same loan held by at least one traded BDC and one NT-BDC in the same quarter.) We also find that, across NT-BDCs, lagged performance is positively correlated with net flows (both fulfilled and requested), driven primarily by inflows.

Taken together, these findings have two potential implications. First, the leverage-valuation relationship may reflect differences in how publicly traded BDCs and NT-BDCs exercise valuation discretion.[4] This could matter for lenders whose asset-backed credit facilities to BDCs (and other private credit vehicles) may reflect these valuation marks (see, e.g., Berry, 2026). Second, redemption pressures may force an NT-BDC's board to choose between gating, which risks signaling distress, and liquidating illiquid loans, which could generate fire-sale externalities. Such externalities are well documented for corporate bond mutual funds (MFs), where net outflows are especially sensitive to poor performance (see, e.g., Goldstein et al., 2017).

Moreover, as NT-BDC *inflows* (rather than gross outflows) are positively correlated with past performance, the performance-driven asset fire-sale channel in corporate bond MFs is probably less salient for NT-BDCs, which can also suspend redemptions. Even so, this pattern creates a different type of liquidity strain: if gross outflows are relatively insensitive to past performance while inflows are not, weaker relative performance would be associated with a wider gap between redemption requests and inflows. As redemptions are funded in part by inflows, the shortfall must be met with cash, credit facilities, or asset sales, posing a similar gating-versus-liquidation tradeoff even without a surge in redemption requests.

[4] To be sure, this is not to suggest that NT-BDCs operate without valuation guardrails; they are subject to the same fair-value framework (ASC 820 and Rule 2a-5), board oversight, and audit requirements as publicly traded BDCs. Our point is that, within this framework, Level 3 valuations still involve meaningful management judgment.

1.1. Related Literature

We contribute to several strands of the literature.

1.1.1. *Liquidity transformation in semi-liquid private credit vehicles*

Most closely related to our paper is recent work by Fang et al. (2026), who examine fragilities in "semi-liquid" BDCs. They show that these funds face run-like dynamics: those experiencing net outflows tend to sell illiquid assets, suffering significant liquidation costs. Moreover, they show that funds with high software exposure and low liquid-asset holdings tend to experience larger outflows, on average. These funds also respond to net outflows by increasing leverage. We complement their analysis by focusing on similar fragilities—opaque, illiquid assets, leverage, and liquidity transformation—but examining a distinct channel: by exploiting the structural differences between NT-BDCs and publicly traded BDCs, we investigate whether higher leverage is associated with incrementally higher loan valuations for NT-BDCs.[5]

1.1.2. *Characteristics of private credit vehicles*

Several papers provide overviews of the private credit industry, including its growth, key players, and potential vulnerabilities (see, e.g., Cai and Haque, 2024; Fillat et al., 2025; Avalos et al., 2025; Preece and Wilson, 2026; Brinkman et al., 2026; and Ivashina, 2026). A related literature documents the growing interconnections between banks and Non-Bank Financial Intermediaries (NBFIs) (see, e.g., Berrospide et al., 2025; Levin and Malfoy-Camine, 2025; and Leigh et al., 2026) and the liquidity characteristics of semi-liquid funds (George and Shin, 2026; Fang et al., 2026). In a Global Financial Crisis-style stress test exercise, Chernenko and Scharfstein (2025) show that no BDC defaults, but BDCs' deleveraging reduces credit provision

[5] Outside academic research, financial stability bodies have also published reports on the potential vulnerabilities of private credit, including linkages to banks (see, e.g., Financial Stability Board, 2026).

by ten percent. We focus specifically on NT-BDCs, exploiting their structural differences from publicly traded BDCs to understand leverage-driven valuation incentives.

1.1.3. *Valuation discretion in illiquid instruments*

Our paper also relates to the literature on valuation discretion and return-smoothing behavior of asset managers (see, e.g., Agarwal et al., 2011; Cici et al., 2011; Kwon et al., 2020; Askhat, 2026; Wilson, 2026; Andrade and Lie, 2026). Daniel et al. (2026) document a "liquidity gradient" in loan valuations: following negative shocks, closed-end BDCs (traded and private) report higher loan prices than semi-liquid BDCs, which in turn report higher loan prices than MFs and exchange-traded funds. This gradient reflects the interactions between loan opacity, which grants managers valuation discretion, and investor redemption rights, which discipline that discretion. Furthermore, they show that, during periods of broad-based stress, leverage is not significantly associated with loan prices; however, leverage is associated with lower prices before default. Our analysis complements theirs by examining this mechanism across distinct structures. Because their closed-end category pools exchange-traded BDCs with private BDCs, neither of which offers redemption at NAV, their estimates do not show whether the leverage association differs with investor liquidity. We examine this by comparing the association between loan valuations and lagged leverage across NT-BDCs and publicly traded BDCs.

1.1.4. *Flow-performance sensitivity*

Finally, we contribute to the broader literature on liquidity transformation risks, which has mostly focused on MFs. This work has evolved from early correlation studies (see, e.g., Spitz, 1970; Ippolito, 1992) to Sirri and Tufano's (1998) canonical empirical finding of equity MFs' asymmetric flow response to performance. In a theoretical model, Berk and Green (2004) show that investor performance-chasing flows can be rational—in equilibrium—under

decreasing returns to scale. Subsequent studies document heterogeneity across investor types (see, e.g., Del Guercio and Tkac, 2002) and between active and passive funds (Anadu et al., 2020) and examine asset fire-sale risks in corporate bond MFs (see, e.g., Chen et al., 2010; Wang, 2015; Goldstein et al., 2017; Falato et al., 2021; Ma et al., 2022). We draw on this literature to examine NT-BDCs' flow-performance sensitivity.

The rest of this paper proceeds as follows. Section 2 provides background information on BDCs and the recent private-market-related stress events. Data and sample statistics are reported in Section 3. Our hypotheses and empirical results are presented in Section 4, and Section 5 concludes.

2. BACKGROUND

2.1. Business Development Companies

Private credit refers to loans from NBFIs that are made directly to small- and middle-market borrowers (for more on the private credit industry, see, e.g., Cai and Haque, 2024; Ivashina, 2026). There are several types of private credit *strategies*, including direct lending, asset-based lending, and mezzanine, distressed, and venture debt. There are also different types of private credit *vehicles*, such as private credit funds, Collateralized Loan Obligations, and BDCs.

BDCs are closed-end funds that choose to be regulated under special provisions of the Investment Company Act of 1940 (1940 Act).[6] Thus, unlike other private credit vehicles that rely on exemptions from the 1940 Act, BDCs are subject to provisions related to investor protection, disclosures, and board governance.

[6] Specifically, Sections 54-65 of the 1940 Act.

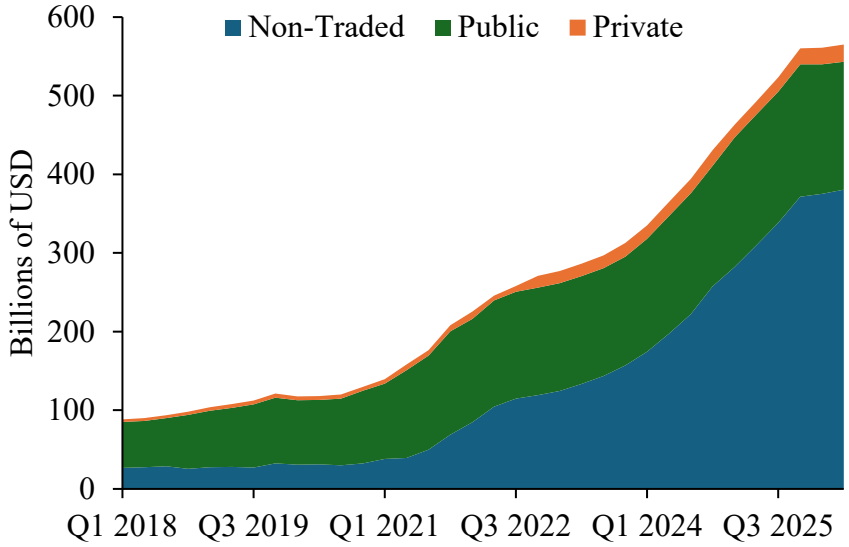
There are several types of BDCs, including (1) publicly traded BDCs, whose shares are traded on national exchanges; (2) private BDCs, which are typically sold through private placements, have a finite term, and do not offer redemptions or continuous subscriptions; and (3) the focus of this paper, perpetual-life, continuously offered NT-BDCs (for more on BDC structures, see, George and Shin, 2026).

NT-BDCs are not *required* to offer share redemptions. Rather, they typically offer discretionary quarterly tender offers to repurchase up to five percent of shares outstanding; subscription frequencies are typically monthly or quarterly. In contrast with publicly traded BDCs, whose shares are exchange-traded like public equities, NT-BDC shares are not traded. Relative to MFs, which *must* offer investors daily redemptions, NT-BDCs engage in less pronounced forms of liquidity transformation. Even so, NT-BDCs invest in more illiquid assets and use more balance sheet leverage than MFs.[7]

NT-BDCs have experienced rapid growth in recent years. Indeed, as reported in Figure 1, NT-BDC assets have risen by approximately $350 billion, or 1,300 percent, since 2018; they now account for 67 percent of all BDC assets, up from 31 percent in 2018. Relative to the private credit industry, NT-BDCs now represent 21 percent of total private credit assets, up from three percent in 2018.

[7] The Level 3-to-total assets ratio for bank loan MFs is about one percent (Anadu et al., 2026). In contrast, over 80 percent of NT-BDCs' holdings are classified as Level 3 assets (Figure 2).

Figure 1: Assets Under Management in BDCs



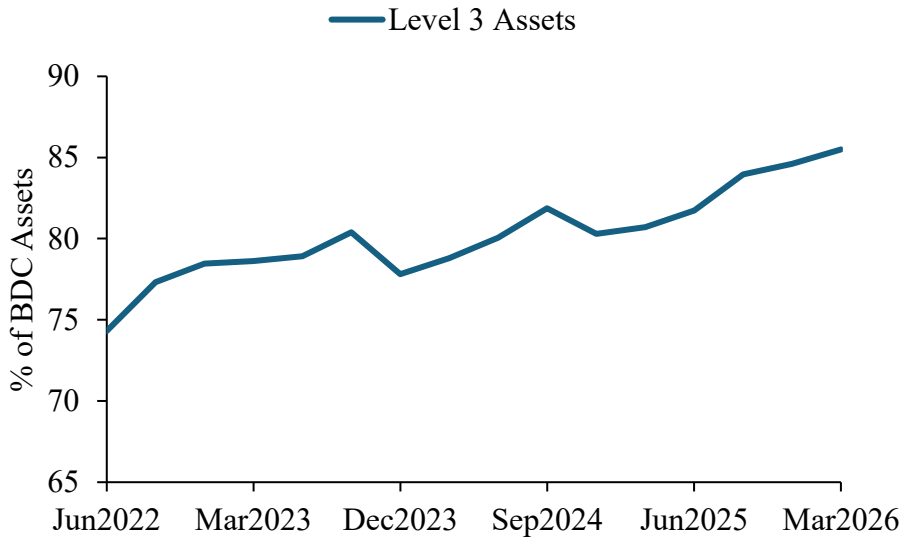
Sources: PitchBook; authors' calculations.
Notes: Assets under Management (AUM) data are based on fair values.

2.2. Asset Liquidity in NT-BDCs

BDCs—and private credit vehicles writ large—hold primarily illiquid loans. Fang et al. (2026) estimate that 78 percent of semi-liquid BDCs' loan portfolio assets are unrated, which tend to be smaller loans and less transparent than rated loans. Figure 2 shows that about 85 percent of NT-BDCs' total assets are classified as Level 3 assets, which are generally illiquid and whose values are derived from unobservable inputs that require management judgment (Financial Accounting Standards Board [FASB], 2006).[8]

[8] This management judgment can be significant (Hohl and Daly, 2026). In contrast, Level 1 assets are valued using unadjusted market quotes, and Level 2 assets are valued using observable inputs other than Level 1 quoted prices (FASB, 2006).

Figure 2: Level 3 Assets of NT-BDCs



Sources: NT-BDCs' 10-K and 10-Q filings; authors' calculations.
Notes: The data consist of the nine largest NT-BDCs with history from 2022 through 2026.

2.3. Heightened Redemptions from NT-BDCs Beginning in Fall 2025

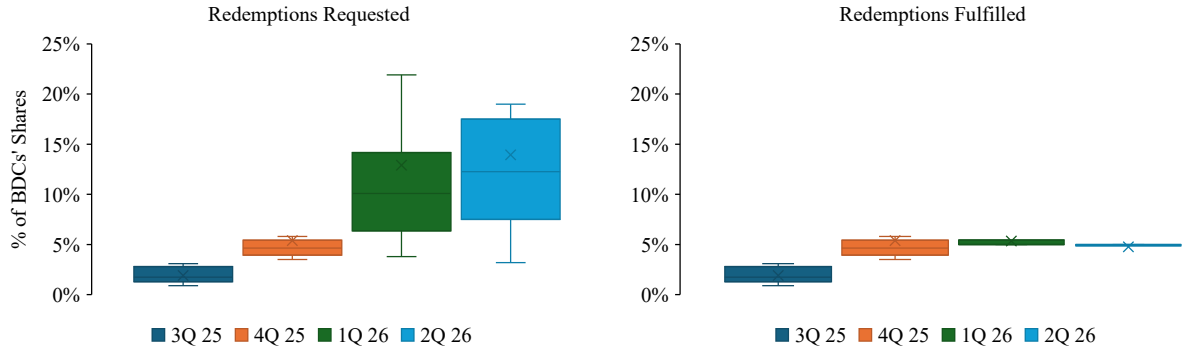
Beginning in September 2025, widespread news of elevated investor redemption requests from NT-BDCs drew heightened attention from regulators and policymakers; media commentary often focused on whether these redemption pressures were signs of broader stresses in the NBFI space. In a sense, the experience of Blue Owl Capital's NT-BDCs became one of the most visible "stress tests" for the NT-BDC model.

In Q4 2025, Blue Owl Technology Income Corp. (OTIC), an NT-BDC concentrated in software investments, experienced heightened redemption requests.[9] In the weeks that followed, NT-BDCs experienced unusually large investor redemption *requests*, averaging 13 percent

[9] Scrutiny of Blue Owl was already elevated after the failed merger of two of its BDCs. Specifically, in November 2025, Blue Owl announced a merger between its NT-BDC, OBDC II, and a publicly traded one, OBDC. Blue Owl suspended redemptions from the NT-BDC pending the merger. Weeks later, following a sharp decline in OBDC's price, Blue Owl cancelled the merger and announced plans to resume its quarterly redemptions in Q1 2026. On February 18, 2026, however, Blue Owl again halted redemptions and began liquidating OBDC II's assets, some of which were sold near par to institutional investors (Blue Owl, 2026).

(Figure 3, left panel). However, most NT-BDCs' fulfilled redemptions were at or near the five percent discretionary redemption cap (Figure 3, right panel).

Figure 3: Redemptions Requested and Fulfilled from Selected NT-BDCs



Sources: BDCs' 10-K and 10-Q filings; authors' calculations.
Notes: The sample consists of the eleven largest NT-BDCs. The horizontal lines inside the boxes show the median values, and the "X" markers show the mean values. The upper and lower whiskers extend to the largest and smallest observations within the third quartile plus 1.5×IQR and the first quartile minus 1.5×IQR, respectively, where IQR is the interquartile range. Outliers are omitted.

3. DATA

We examine two questions. First, does the leverage-valuation relationship differ between NT-BDCs and publicly traded ones? Second, to what degree do investors in NT-BDCs respond to past performance?

To answer both questions, we obtain quarterly balance sheet data on BDCs, including total assets, total liabilities, and Level 3 assets, from their 10-K and 10-Q filings with the Securities and Exchange Commission (SEC). We augment these aggregated data with portfolio holdings information—such as loan fair value, Payment-in-Kind (PIK), and accrual status—from PitchBook. Our sample runs from 2018 to 2026 and includes (1) the 11 largest NT-BDCs as of Q4 2025, which account for 70 percent of the NT-BDC universe; and (2) 30 publicly traded BDCs, which account for roughly 75 percent of the publicly traded BDC universe, as of June 2026.

3.1. Summary Statistics

Table 1 reports summary statistics for the NT-BDC and traded BDC sample used to address question one. On average, NT-BDCs are substantially larger than traded BDCs. Moreover, NT-BDCs tend to have lower leverage (asset-to-equity), Level 3 assets, software concentration, nonaccruals, and PIK rates than publicly traded ones.[10] Loan valuations are marginally lower, on average, for NT-BDCs than for traded BDCs. On average, each loan in our sample is held by about three BDCs, across traded and non-traded BDCs.

Table 1: Summary Statistics of Selected Variables (1/2)

Variable	Non-traded (1)	Traded (2)	Difference (3)
Loan Valuation (cents/$)	95.7 (12.3)	96.4 (11.2)	-0.7***
Leverage (%)	188.0 (24.8)	209.0 (24.4)	-21***
Level 3 Assets (%)	75.2 (12.3)	90.2 (9.1)	-15.0***
AUM ($bil)	20.4 (22.7)	6.0 (5.8)	14.4***
Software Concentration (%)	24.5 (8.3)	26.6 (16.3)	-2.1***
Number of BDCs per Loan	3.2 (1.7)	3.1 (1.6)	0.1***
Nonaccruals (%)	0.6 (0.8)	1.9 (2.0)	-1.3***
PIK (%)	5.9 (3.1)	9.6 (5.0)	-3.7***

Sources: BDCs' 10-K and 10-Q filings; authors' calculations.
Notes: This table reports the averages (standard deviations) for selected variables for non-traded (column 1; n=11) and traded (column 2; n=30) BDCs. Leverage is computed as the ratio of assets to equity. Column 3 reports the difference between non-traded and traded BDCs. The data are quarterly averages from 2018 through 2026. The ***, **, and * indicate, respectively, statistical significance at the 1 percent, 5 percent, and 10 percent levels.

[10] As shares of traded BDCs are bought and sold on exchanges, not at NAV, traded BDCs do not engage in liquidity transformation, i.e., they need not liquidate underlying loans in response to shareholder redemption activity. Thus, traded BDC managers may be incentivized to hold more (less liquid) Level 3 assets (see, Table 1) than their NT BDC peers.

Summary statistics for the sample used for question two are reported in Table 2. Fulfilled net flows are more positive than requested net flows because NT-BDCs mostly gated redemptions (outflows) exceeding five percent. Due to the rapid growth of NT-BDCs since 2021, inflows exceed fulfilled and requested redemptions by a large margin. The average performance is about 2.2 percent per quarter over the sample period.

Table 2: Summary Statistics of Selected Variables (2/2)

Variable	Mean (Std. Deviation)
Fulfilled Net Flows (%)	13.4 (15.5)
Requested Net Flows (%)	12.4 (17.0)
Inflows (%)	15.5 (14.5)
Fulfilled Redemptions (%)	2.1 (1.7)
Requested Redemptions (%)	3.1 (5.4)
Performance (%)	2.2 (1.1)
AUM ($bil)	14.3 (18.6)
Leverage (%)	184.0 (25.3)
Level 3 Assets (%)	75.0 (14.5)
Liquidity (%)	38.4 (18.2)

Sources: BDCs' 10-K and 10-Q filings; authors' calculations.
Notes: This table reports the averages (standard deviations) for selected variables for non-traded BDCs. The data on net flows and performance are winsorized at the 5 percent level, and the data are quarterly averages from 2018 through 2026.

Next, we examine both questions empirically in Section 4.

4. EMPIRICAL ANALYSIS

Hypothesis 1: *The relationship between fund leverage and loan valuation is more positive for NT-BDCs than for publicly traded BDCs, on average.*

4.1. Motivation; Differences Between Traded and NT-BDCs

Publicly traded BDCs and NT-BDCs invest in similar—and relatively illiquid—assets, but there are important structural differences between the two vehicles. NT-BDC shares do not trade on the secondary market; thus, market-based price data are not available for NT-BDCs. In contrast, a publicly traded BDC has two prices: a secondary-market price and NAV, which is the value of its underlying assets less liabilities, divided by shares outstanding. Accordingly, publicly traded BDCs may trade at premiums or discounts to their NAV; these spreads reflect, in part, investors' views on the value of the fund's net assets, as well as its liquidity and credit quality, among other factors.[11]

Against this backdrop, we ask: does the relationship between leverage and valuation differ across BDC structures?[12] To be sure, both traded and NT-BDC managers face similar exposures to reported valuations: loan marks impact their asset coverage test (i.e., regulatory leverage caps) and fee revenues, which are a function of assets.[13] However, this exposure is likely greater for NT-BDCs through at least two channels.

First, an NT-BDC's NAV is the price at which investors buy and sell shares, rather than a reference point alongside a market price. Therefore, loan markdowns *directly* affect an NT-BDC's reported returns. In contrast, traded BDC investors transact at a market price that reflects,

[11] Matvos et al. (2026) document that publicly traded BDCs' market prices decline faster than their reported NAVs and that the market price-NAV gap becomes larger during periods of stress.
[12] We focus specifically on the *slope* of loan valuations conditional on leverage, not their levels.
[13] All BDCs value their loans within a common framework of board oversight, fair value accounting standards, and external audit. Specifically, under SEC Rule 2a-5, a fund board is responsible for fair value determinations and may designate the adviser to perform them, subject to its oversight. Valuations must also comply with FASB ASC 820.

in part, the market's view of the value of the BDC's assets. Accordingly, generous valuation marks offer less benefit to traded BDCs.[14] Second, as leverage mechanically amplifies the effects of asset markdowns on equity NAV, the equity cost of a markdown is likely greater, on net, for more levered NT-BDCs (see Daniel et al., 2026). This gives managers of more highly levered NT-BDCs a stronger incentive to maintain (more) generous valuations than managers of traded BDCs.[15,16]

4.2. Empirical Specification

To test our hypothesis, we estimate the following quarterly regression:

$$Valuation_{i,m,t} = \beta_0 + \beta_1 Leverage_{m,t-1} + \beta_2 NT\ BDC\ Dummy_{m,t} + \boldsymbol{\beta_3} Leverage_{m,t-1} * NT\ BDC\ Dummy_{m,t} + \gamma\ Controls + FE + \varepsilon_{i,m,t} \quad (1)$$

where $Valuation_{i,m,t}$ is the ratio of fair value to principal for loan *i* held by BDC *m* at time *t.*[17] Importantly, we restrict the sample to loans held by at least two BDCs in the same quarter; this requires exact matches on various identifiers, including loan ID number, loan maturity, and loan type. This conservative identification strategy yields loans representing almost three percent of total outstanding loans held by BDCs by count, but ten percent by value, as of June 2026.[18]

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[14] Traded BDC managers may also mark loans more conservatively because the discount to NAV disciplines them. Alas, our empirical test cannot separate these two factors.

[15] For a given asset markdown, the percentage NAV decline scales with the fund's asset-to-equity (leverage) ratio. Formally, if Equity (NAV) = Assets – Liabilities, then %Δ NAV ≈ (Assets/Equity) × %Δ Assets.

[16] Also, BDCs borrow against their loan values and must satisfy a 200 percent (or, if elected, 150 percent) asset coverage ratio. Thus, higher loan valuations can boost borrowing capacity—and reduce leverage ratios—creating an incentive to delay or mute markdowns in response to negative shocks (Daniel et al., 2026). It is unclear whether this incentive is stronger for NT-BDCs than traded BDCs. The asset coverage ratio is computed as total assets, less non-debt liabilities, divided by total senior securities.

[17] We compute Valuation as Fair Value divided by Principal rather than as the ratio of Fair Value to Cost. We do so because Cost can embed prior write-downs, PIK accruals, and origination discounts, making it an inconsistent benchmark across loans and over time. Principal, in contrast, is a fixed, objective measure of the contractual claim, so scaling by principal more cleanly isolates manager valuation discretion.

[18] Some of these loans are held only by traded BDCs or only by NT-BDCs. Nonetheless, with Loan × Date fixed effects, the NT Dummy is identified from loans held by both types of BDCs, while the leverage slopes also use variation among BDCs of the same type.

$Leverage_{m,\,t-1}$ is the asset-to-equity ratio for fund m at time t-1. $NT\ BDC\ Dummy_{m,t}$ is an indicator variable that is equal to 1 if the fund is an NT-BDC and 0 otherwise. Because we are interested in the incremental association between leverage and loan valuation for NT-BDCs relative to traded ones, the coefficient of interest is β_3, the interaction between the NT-BDC dummy variable and lagged leverage.

We control for several BDC- and loan-level characteristics, including the lagged Level 3-to-total-assets ratio, lagged log AUM, portfolio-level nonaccrual and PIK shares, and the number of BDCs holding a specific loan in the same quarter. We include loan fixed effects to absorb time-invariant loan characteristics, such as industry, and time fixed effects to control for macroeconomic and market-wide factors common to all BDCs. In our main specification, we replace these with Loan × Date fixed effects, which also absorb time-varying credit quality, so that identification comes from differences in marks on the same loan at the same date. Standard errors are clustered two-way at the loan and BDC levels.

4.3. Results

Table 3 reports our results on the relationship between leverage and valuation for NT-BDCs. In our baseline regression without time or loan fixed effects (Column 1), on average, a one-percentage-point increase in lagged leverage is associated with an additional increase in loan valuation of 0.06 cents per USD (six basis points) for NT-BDCs relative to traded BDCs.

In our main specification with Loan x Date fixed effects (Column 3), the effect is around 0.05 cents per USD and is statistically significant at the five percent level. This suggests that NT-BDC valuations are more positively associated with leverage than those of traded BDCs, after controlling for BDC-level characteristics and Loan × Date fixed effects. To be sure, we do

not have any external price benchmark. Thus, this pattern is consistent with, but does not isolate, valuation discretion.[19]

This effect is sizeable: for an NT-BDC, on average, a one-standard-deviation increase in leverage (about 25 percentage points; Table 1) is associated with an additional 1.15 cents per USD increase in loan valuation relative to traded BDCs (using the unrounded coefficient). For comparison, the mean (median) standard deviation of valuations by loan and quarter is 3.4 (0.58) cents per USD. Thus, this effect is about one-third of the mean within loan-quarter standard deviation of valuations, and about twice the median.

Our results are similar in magnitude, albeit less precisely estimated, when we restrict our sample to loans held by at least one traded and one non-traded BDC in the same quarter, as reported in Appendix 1.

[19] The coefficient on Lag Leverage, which captures the relationship for traded BDCs, is negative. This may reflect, in part, a negative mechanical correlation: BDCs that persistently mark their loans higher report higher NAVs and, thus, lower leverage. The interaction with the Non-Traded Dummy more than offsets this negative correlation. Because leverage is centered, the coefficient of the Non-Traded Dummy measures the valuation difference between an NT-BDC and a traded BDC at average leverage for the same loan in the same quarter.

Table 3: Loan Valuation and Lagged Leverage

Dependent Variable (cents/$):	Loan Valuation (1)	Loan Valuation (2)	Loan Valuation (3)
Lag Leverage	-0.03	-0.02*	-0.03**
	(0.02)	(0.01)	(0.01)
Non-Traded Dummy	-2.28	-1.99**	-2.07**
	(1.71)	(0.93)	(0.98)
Lag Leverage * Non-Traded Dummy	0.06*	0.04**	0.05**
	(0.03)	(0.02)	(0.02)
Lag Level 3 Assets	-0.06	-0.03	-0.04*
	(0.04)	(0.02)	(0.02)
Lag Log AUM	0.68**	-0.02	-0.05
	(0.34)	(0.20)	(0.21)
Number of BDCs per Loan	0.57***	0.13	
	(0.13)	(0.12)	
Nonaccrual	-0.31*	-0.18**	-0.19*
	(0.18)	(0.08)	(0.10)
PIK	0.09	0.02	0.00
	(0.08)	(0.06)	(0.07)
Loan	No	Yes	No
Date	No	Yes	No
Loan x Date	No	No	Yes
S.E. Clustered	Loan + BDC	Loan + BDC	Loan + BDC
n	25477	25338	24726
R^2	0.018	0.592	0.711

Sources: BDCs' 10-K and 10-Q filings; PitchBook; authors' calculations.
Notes: Loan Valuation is defined as Fair Value over Principal (cents/$). Lag Leverage is the lagged asset-to-equity ratio (%) and is centered at the mean. Non-Traded Dummy equals one if the BDC is a perpetual-life, non-traded fund. Lag Level 3 Assets is the lagged share of total assets (%). Lag Log AUM is the natural log of lagged total assets under management ($). Number of BDCs per Loan is the number of BDCs holding a given loan in the same quarter; it is omitted from column (3) due to collinearity with Loan × Date fixed effects. Nonaccrual and PIK are BDC-quarter averages of loan-level nonaccrual and payment-in-kind status (%). Standard errors are two-way clustered by loan and BDC and are reported in parentheses. The ***, **, and * indicate, respectively, statistical significance at the 1 percent, 5 percent, and 10 percent levels.

We employ several design features to address distinct identification concerns. First, lagging leverage partly mitigates reverse causality between contemporaneous valuations and leverage. Second, loan, date, and Loan × Date fixed effects absorb time-invariant loan characteristics and time-varying market-wide shocks, mitigating omitted variable bias. (The

Loan × Date specification provides the strongest identification by exploiting within-loan-quarter variation across BDCs holding the same loan simultaneously.) Finally, two-way clustering of standard errors by loan and BDC accounts for the panel structure of our data, addressing concerns about correlated residuals.

Hypothesis 2: *There is a positive relationship between an NT-BDC's past performance and investor flows, on average.*

4.4. Motivation; BDCs versus Mutual Funds

The MF literature shows that investors respond to past performance: the relationship is convex for equity MFs (see, e.g., Sirri and Tufano, 1998; Chevalier and Ellison, 1997) and concave for corporate bond MFs (Goldstein et al., 2017) and for equity MFs holding illiquid assets (Chen et al., 2010).[20] Drawing on this robust literature, we investigate whether investors in NT-BDCs are responsive to past performance and, if so, the shape of that response curve.

To be sure, there are important structural differences between MFs and NT-BDCs, which limit comparability between the two products. For example, all MFs, including those that invest in relatively illiquid debt, must offer daily redemptions at NAV; this creates liquidity transformation risks and fire-sale vulnerabilities (see, e.g., Anadu and Cai, 2019; Anadu et al., 2026; Falato et al., 2021; Goldstein et al., 2017). In contrast, NT-BDCs offer *discretionary* redemptions—typically quarterly and capped at five percent of their shares outstanding.[21] Thus,

[20] A convex flow-performance relationship means that flows are more sensitive to good performance than to poor performance; Sirri and Tufano (1998) attribute this pattern to search costs, which lead investors to concentrate inflows in the most visible top performers. In contrast, a concave relationship means that flows are more sensitive to poor performance; Goldstein et al. (2017) attribute this pattern to the illiquidity of corporate bonds, which creates strategic complementarity among redeeming investors.

[21] In theory, an NT-BDC that is facing redemption requests greater than five percent could choose to suspend all redemptions, although, in practice, most have maintained the five percent cap. MFs, on the other hand, must meet all requested redemptions daily. In deciding how to meet redemption requests, an NT-BDC manager must balance preserving the fund's liquidity today against the future effects of gating on its franchise value. Examining these tradeoffs is beyond the scope of this paper.

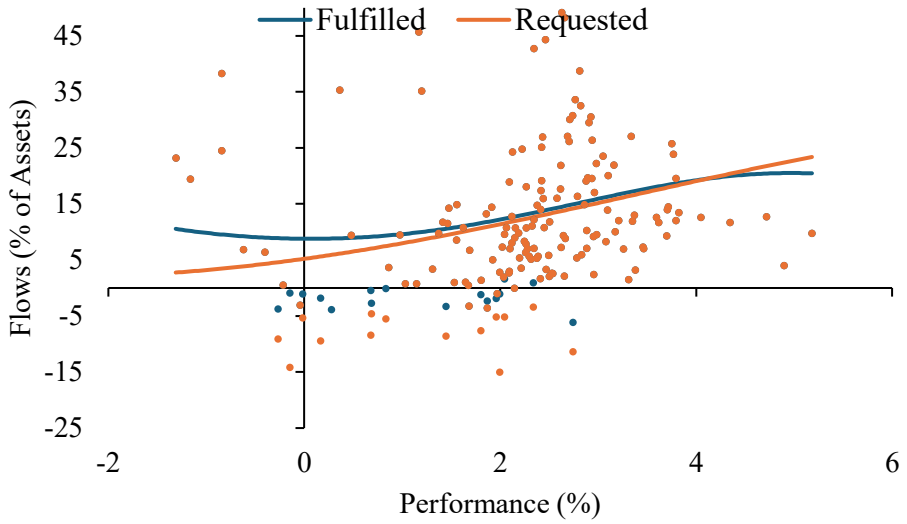
while both fund types engage in liquidity transformation, NT-BDCs' ability to gate and suspend redemptions provides a potential fire-sale escape valve. (That said, theoretical and empirical evidence from money market funds suggests that redemption gates [and fees] can trigger preemptive runs and signal distress [Cipriani et al., 2014; Li et al., 2021].)

Even so, we study this question because understanding whether redemption caps defer, rather than prevent, potential fire sales is important for financial stability monitoring. Sustained redemption *requests*—even if they do not manifest in *actual* redemptions due to the cap—could reveal investor concerns about NT-BDCs' portfolios. This, in turn, could signal rising concerns in the broader private credit markets. Moreover, if NT-BDCs meet heightened redemption requests by selling illiquid loans or reducing lending, stress could propagate to the broader corporate credit market. For example, fire-sale-induced loan markdowns from one NT-BDC could impact other entities that hold the same or similar loans—or prompt further redemptions from NT-BDCs (Matvos et al., 2026).

To further motivate our analysis, Figure 4 compares nonparametric local linear regression estimates for fulfilled and requested net flows.[22] While both measures display a positive gradient between lagged performance and flows, the slope for fulfilled net flows flattens in the negative-performance region. One potential interpretation is that investors want to redeem more after poor performance (or episodes of heightened stress), but redemption caps mechanically prevent them from doing so.

[22] Inflows are defined as the number of shares purchased during a quarter divided by the lagged number of shares outstanding, as reported in a BDC's 10-Q or 10-K filings. Fulfilled (requested) outflows are the number of shares repurchased (requested for repurchase) during a quarter divided by the lagged number of shares outstanding. When current-quarter data are not yet available in the 10-Q or 10-K filings, we use Schedule TO-I/A (tender offer statements) or 8-K (current reports) filings. Fulfilled (requested) net flows equal inflows minus fulfilled (requested) outflows. Redemptions fulfilled or requested are assigned to the quarter in which the corresponding tender offer concluded.

Figure 4: Net Flows to Lagged Performance for NT-BDCs



Sources: BDCs' 10-K and 10-Q filings; authors' calculations.
Notes: This figure plots local linear kernel regression estimates of net flows on lagged quarterly performance, estimated separately for fulfilled and requested net flows, using a second-order Gaussian kernel following Hayfield and Racine (2008). Bandwidths were selected via least-squares cross-validation and scaled by a factor of 10 for visual smoothing. In most cases early in the sample period, NT-BDCs fulfilled all redemption requests, causing fulfilled and requested data points to overlap.

4.5. Empirical Specification

To test our hypothesis, we estimate the following quarterly equation:

$$Flow_{m,t} = \beta_1 \, Lag_Performance_{m,t-1} + \gamma \, Controls + FE + \varepsilon_{m,t} \quad (2)$$

where $Flow_{m,t}$ is one of the following quarterly measures: (1) *fulfilled* net flows; (2) *requested* net flows; (3) gross inflows; (4) *fulfilled* gross outflows; and (5) *requested* gross outflows. "Fulfilled" measures actual net and gross redemptions (share repurchases) made by the BDC, whereas "Requested" measures the gross and net amounts of redemptions that would have occurred had all requests been fulfilled. $Lag_Performance_{m,t-1}$ denotes the quarterly percentage change in NAV per share plus distributions paid per share.

We include lagged flows to address serial correlation, and we control for lagged log AUM, lagged leverage, lagged Level 3 assets, and lagged liquidity. BDC and time fixed effects isolate the within-fund relationship between performance and flows. (Time fixed effects also

absorb sector-wide shocks. Thus, the estimates reflect cross-sectional fund differences within a quarter.)

4.6. Results

Our results are reported in Table 4. Columns 1 and 2 show, respectively, that a one-percentage-point increase in lagged performance is associated with increases of 2.3 and 2.6 percentage points in *fulfilled* and *requested* net flows, on average. However, this effect is driven by inflows (2.5 percentage points for inflows, Column 3), as gross redemptions—both fulfilled (Column 4) and requested (Column 5)—are not significantly correlated with lagged performance.

Taken together, these findings suggest that NT-BDC fragility may differ from the run-like dynamics in daily-redeeming corporate bond MFs, where concave flow-performance relationships can amplify asset fire sales. Here, the responsiveness of net flows to performance comes primarily from inflows. Thus, weak fund performance could dampen inflows that funds may rely on, in part, to meet redemptions.

A second potential implication concerns what drives redemptions. Redemption requests are not significantly related to past performance but are related to lagged redemption requests (Column 5), whereas fulfilled repurchases are not (Column 4).[23] Thus, redemption demand appears persistent and constrained by repurchase caps. It may respond more to sector-wide shocks, such as the 2025 software shock documented by Fang et al. (2026), than to relative performance.

[23] Redemption requests may be positively correlated with redemption requests in period t-1, as gating requests at five percent may leave a residual of unfulfilled redemption requests from investors who may then submit them again in the following tender offer period.

Table 4: Net Flows and Lagged Performance

Dependent Variables (%):	Fulfilled Net Flows (1)	Requested Net Flows (2)	Inflows (3)	Redemptions Fulfilled (4)	Redemptions Requested (5)
Lag Performance	2.26*	2.58**	2.48**	0.14	-0.13
	(1.21)	(1.19)	(1.14)	(0.13)	(0.24)
Lag Flows	0.08	0.14**	0.07	0.06	1.58***
	(0.06)	(0.06)	(0.06)	(0.11)	(0.23)
Lag Log AUM	-23.52***	-21.99***	-23.34***	0.42	-0.02
	(5.69)	(5.57)	(5.60)	(0.25)	(0.38)
Lag Leverage	0.12**	0.14**	0.13**	0.01**	-0.01
	(0.06)	(0.05)	(0.06)	(0.00)	(0.01)
Lag Level 3 Assets	-0.12	-0.07	-0.13	-0.00	-0.04
	(0.11)	(0.11)	(0.11)	(0.01)	(0.03)
Lag Liquidity	-0.22**	-0.36***	-0.22***	-0.00	0.04*
	(0.08)	(0.08)	(0.07)	(0.01)	(0.02)
Date	Yes	Yes	Yes	Yes	Yes
BDC	Yes	Yes	Yes	Yes	Yes
S.E. Clustered	Time	Time	Time	Time	Time
n	166	166	166	166	166
R^2	0.83	0.85	0.82	0.80	0.86

Sources: BDCs' 10-K and 10-Q filings; PitchBook; authors' calculations.
Notes: Fulfilled (Requested) Net Flows is defined as Inflows minus actual (requested) Outflows, scaled by lagged shares outstanding (%). Inflows, Redemptions Fulfilled, and Redemptions Requested are the respective elements separated out of Net Flows. Lag Performance is the change in NAV per share plus distributions per share paid out during the quarter, scaled by lagged NAV per share. Lag Flows is the one-quarter lag of the dependent variable. Lag Leverage is the lagged asset-to-equity ratio (%). Lag Level 3 Assets is the lagged share of total assets(%). Lag Liquidity is the lagged sum of cash and available credit, divided by net assets (%); when a BDC reports only undrawn (rather than total available) credit, available credit is imputed using the average ratio of undrawn-to-available credit reported by other BDCs in the same quarter. Standard errors are clustered by time and are reported in parentheses. The ***, **, and * indicate, respectively, statistical significance at the 1 percent, 5 percent, and 10 percent levels.

Several design features mitigate autocorrelation and omitted variable bias concerns. First, we include lagged flows to absorb persistence in fund flows and reduce bias from the dynamic structure of the data. Second, BDC fixed effects control for time-invariant, fund-specific heterogeneity. Third, time fixed effects absorb period-specific shocks common to all funds.

4.7. Linking H1 (Loan-Valuation) and H2 (Flow-Performance Sensitivity)

Our two analyses examine potentially reinforcing fragility mechanisms. We show that the leverage-valuation slope is more positive for NT-BDCs than for traded BDCs on the same loan in the same quarter. If these marks are generous, they could, on balance, boost reported NAV and performance. If investors respond to this improved performance by buying more shares, declining performance could slow inflows. At the same time, if performance deteriorates amid other shocks—such as those related to software exposure (Fang et al., 2026)—redemption requests could rise.

Faced with redemption requests in excess of the five percent cap, a fund's board chooses from a continuum of options: suspend all redemptions, prorate to the five percent cap, or honor all requests. The first two are degrees of gating, which could signal distress at the fund level and, if multiple funds face similar constraints, at the industry level. Redeeming more than the cap may require liquidating loans, which could generate fire-sale externalities. We leave a more robust examination of how these channels interact dynamically to future research.

5. CONCLUSION

The rapid growth of NT-BDCs, combined with the significant redemption pressure beginning in fall 2025, raises critical questions about valuation discretion and investor flow dynamics in these vehicles. We provide evidence on two potential fragility channels. First, by exploiting the structural differences between NT-BDCs and publicly traded BDCs, we find that higher leverage is associated with incrementally higher loan valuations for NT-BDCs relative to publicly traded BDCs holding the same loans. Second, NT-BDC net flows, both fulfilled and requested, are positively associated with past performance, driven by inflows.

Two potentially self-reinforcing implications emerge. First, if higher valuations at more levered NT-BDCs reflect generous loan marks, they could create a first-mover advantage. As NT-BDC investors redeem at NAV, early redeemers may exit at NAVs that do not yet reflect losses, externalizing costs to remaining investors. To be sure, redemption caps act as structural brakes on redemptions; however, they may also prompt preemptive redemption requests (Cipriani et al., 2014). If meeting these requests requires selling illiquid loans below reported values, the resulting losses would further reduce NAV and boost redemption incentives.

Second, because private credit portfolios share common exposures and inflows are positively related to performance, deteriorating performance could generate correlated drops in inflows across many NT-BDCs. If redemption caps bind sector-wide, then fulfilled redemptions would be muted, but the growing backlog of requested redemptions could signal building stress in the private credit markets.

As NT-BDCs grow, understanding valuation practices and the sensitivity of investor flows to past performance becomes increasingly important for financial stability monitoring.

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7. APPENDICES

Loan Valuations and Leverage
(Sample Restricted to Loans Held by at least One Traded and One NT-BDC)

Dependent Variable (cents/$):	Loan Valuation	Loan Valuation	Loan Valuation
Lag Leverage	-0.04	-0.01	-0.01
	(0.03)	(0.02)	(0.02)
Non-Traded Dummy	-3.24	-1.88	-1.87
	(2.04)	(1.25)	(1.30)
Lag Leverage * Non-Traded Dummy	0.07*	0.04*	0.04*
	(0.04)	(0.02)	(0.02)
Lag Level 3 Assets	-0.08	-0.03	-0.04
	(0.05)	(0.03)	(0.03)
Lag Log AUM	-1.05**	-0.00	-0.01
	(0.46)	(0.26)	(0.26)
Number of BDCs per Loan	0.58***	0.01	
	(0.11)	(0.13)	
Nonaccrual	-0.28	-0.04	-0.08
	(0.24)	(0.11)	(0.13)
PIK	0.06	-0.02	-0.00
	(0.10)	(0.08)	(0.09)
Loan	No	Yes	No
Date	No	Yes	No
Loan x Date	No	No	Yes
S.E. Clustered	Loan + BDC	Loan + BDC	Loan + BDC
n	16152	16048	15627
R^2	0.026	0.622	0.724

Sources: BDCs' 10-K and 10-Q filings; PitchBook; authors' calculations.
Notes: Loan Valuation is defined as Fair Value over Principal (cents/$). Lag Leverage is the lagged asset-to-equity ratio (%). Non-Traded Dummy equals one if the BDC is a perpetual-life, non-traded fund. Lag Level 3 Assets is the lagged share of total assets (%). Lag Log AUM is the natural log of lagged total assets under management ($). Number of BDCs per Loan is the number of BDCs holding a given loan in the same quarter; it is omitted from column (3) due to collinearity with Loan × Date fixed effects. Nonaccrual and PIK are BDC-quarter averages of loan-level nonaccrual and payment-in-kind status (%). Standard errors are two-way clustered by loan and BDC and are reported in parentheses. The ***, **, and * indicate, respectively, statistical significance at the 1 percent, 5 percent, and 10 percent levels.