

Media Release

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With equity valuations stretched, private credit offers portfolio protection

As valuations continue to reach record highs, investors should be cautious of concentrating too much of their portfolio in listed equities, according to Tanarra Credit Partners (TCP) managing partner, Peter Szekely.

He says investors should consider corporate private credit which offers structural features that help insulate portfolios from market volatility.

"With equity valuations stretched, corporate private credit offers a compelling alternative investment opportunity. It provides investors with active management and an underwriting discipline supported by structural protections and rigorous selection standards, unlike passive exposure to index-heavy equities."

He says listed equity P/E ratios remain at all-time highs, prompting concerns about whether these valuations are sustainable.

"As of September 2025, the S&P 500 was trading at a trailing price-to-earnings ratio of 27.29, well above its rolling five-year average of 22.17 and its twenty-year average of 16.13. The MSCI World was trading at a P/E ratio of 23.94, also above its five-year average of 20.41."

Mr. Szekely also points to the equity market domination in the US by the 10 largest stocks by market capitalisation, which account for approximately 40 per cent of the S&P 500.

"This is the highest concentration level in the past thirty years. These ten include the big techs, or hyperscalers, Microsoft, Apple, Amazon and Alphabet."

And although not completely dominated by tech, he says the Australian equity market is displaying similar trends with its trailing price-to-earnings ratio also well above historical averages in September at 20.87. In addition, the ASX/S&P 200 surpassed 9000 for the first time last quarter.

"This rally has not been driven by earnings growth, with the median ASX 200 consensus earnings-per-share steadily declining and FY25 consensus earnings growth forecast standing at -1.7 per cent. Instead, growth in the market appears to be driven by a mix of optimism around further interest rate cuts increasing the attractiveness of equities, and international investors looking to decrease their US market exposure.

"Investors that put all their eggs in the equity basket expose themselves to a variety of risks, the most obvious of which is volatility. They are also vulnerable to limited return upside if they buy equities at stretched valuations and correlation risk. Even if stocks are diversified across sectors and industries, all equities can exhibit high levels of correlation during an economic downturn.



"In contrast, mid-market corporate private credit loans have characteristics that can insulate a portfolio from the risk of stretched public equities. For a start, value is derived from credit fundamentals, not market sentiment," says Mr. Szekely.

He says many mid-market corporate private credit loans are underwritten based on the financial performance (specifically, cashflow) and credit worthiness (for example, leverage and interest coverage) of a company. While future growth is considered, private credit valuation and returns centre around business fundamentals rather than volatile factors such as public trading multiples.

"Most loans also include at least one financial covenant, such as a leverage ratio, which provides an early warning sign of underperformance. This provides investors with the ability to work with management and restructure the loan if required. Listed equities provide no similar remedy for investors to preserve value.

"Loans that are senior secured over the cashflow and assets of the company, and supported by a more than 50 per cent equity first-loss position, also offer an extra layer of protection.

"In these scenarios, recovery value on invested capital is primarily tied to the cashflows and assets of the company and overall enterprise value. With an equity first-loss position, a borrower's enterprise value would need to decline by over 50 per cent before the investor's debt is at risk of impairment, providing significant downside protection.

"In the case of the TCP Private Debt Income Fund we take a disciplined approach to capital preservation by taking a senior secured position in loans, having a significant equity first-loss position (50 per cent plus), and maintaining financial covenants that provide important downside protection to investors," he says.

The fund invests in a diversified loan book with a focus on mid-market Australian and New Zealand corporates in defensive sectors with strong tailwinds, such as childcare, IT and financial services and has no exposure to real estate.

"Regardless of how they invest, the combination of diversification benefits, and attractive risk adjusted returns, makes corporate private credit a compelling option for investors seeking stable cash yields in an uncertain economic environment, marked by heightened volatility and stretched valuations," says Mr Szekely.

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