

Introduction to specialty credit

May 2026

Specialty credit has gained attention within the private credit universe in recent years. While direct lending remains the most established private debt strategy, specialty credit offers exposure to a broader set of opportunities. It centers on transactions backed by pools of collateral, where repayment depends primarily on the performance and contractual cash flows of underlying assets rather than a borrower's projected EBITDA.

As a result, it can provide diversification benefits and attractive risk-adjusted returns within a credit portfolio. Despite its growing relevance, specialty credit remains relatively underexplored compared with traditional private debt strategies. In this paper, we introduce specialty credit, including its key characteristics, investment rationale, and role within credit portfolios.

What is specialty credit?

Specialty credit represents a broad and evolving segment of private credit that extends beyond traditional corporate lending (Figure 1). It mostly centers around asset-backed strategies, where repayment depends primarily on the value and cash flows of underlying collateral rather than a corporate borrower's earnings:

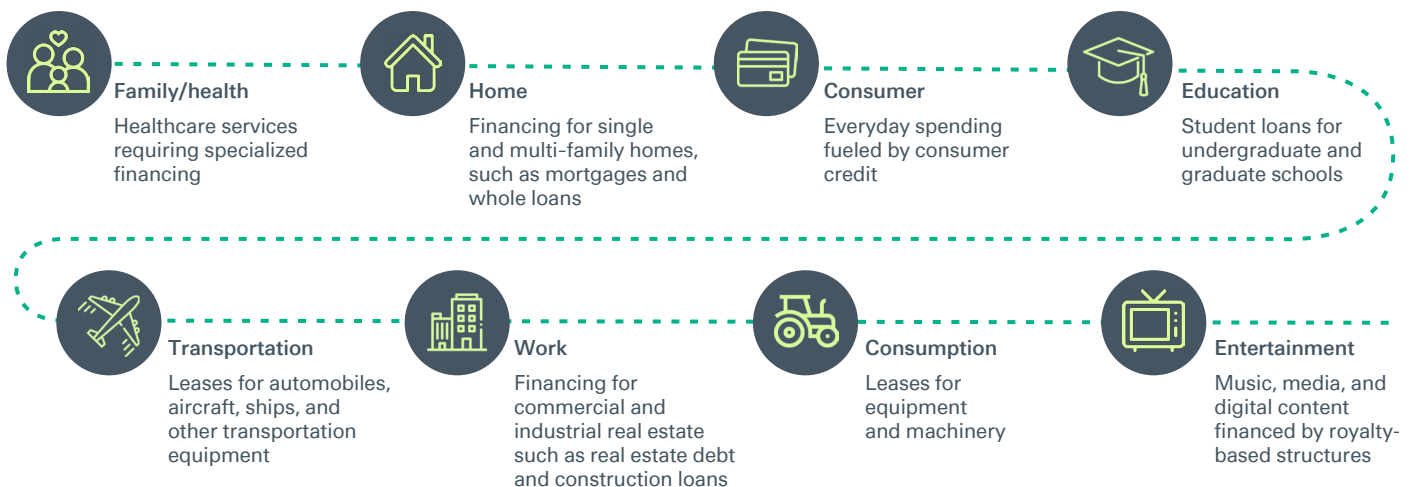
- **Asset-backed lending (ABL):** loans made to businesses secured by hard or financial assets
- **Asset-based finance (ABF):** a broad term for financing arrangements secured by assets, including (whole) loans, securitizations, leasing, factoring, etc.

Specialty credit investing therefore places greater emphasis on collateral quality, cash flow durability, structural protections, servicing capabilities, and the legal framework supporting the assets. This differs from direct lending, where underwriting focuses on a company's earnings and ability to generate future operating cash flows.

Importantly, specialty credit is not a single, homogeneous strategy, but rather a broad ecosystem of sub-strategies spanning hard assets, financial assets, and selected forms of corporate exposure. The opportunity set includes equipment leasing, aviation finance, consumer lending, royalties, litigation finance, NAV lending, and residential and commercial mortgages, among others. Many of these assets are closely tied to everyday economic activity and exhibit quality return drivers across sectors.

Beyond the diversity of underlying assets, specialty credit also differs from traditional corporate lending in the structure and timing of cash flows. Many transactions are backed by self-amortizing asset pools that return principal progressively as underlying assets generate cash flows. This contrasts with typical direct lending loans, where investors receive periodic interest payments and depend on a refinancing, sale, or other liquidity event for a large bullet repayment at maturity. Specialty credit investments often exhibit a more front-loaded cash flow profile, reducing exposure earlier in the investment lifecycle and helping portfolios naturally de-risk over time.

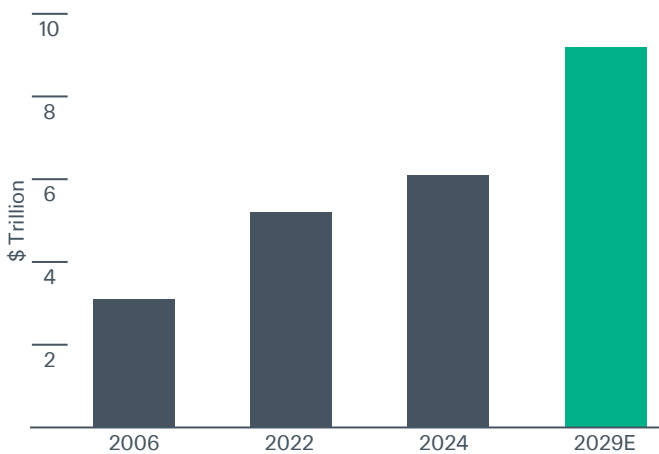
FIGURE 1: SPECIALTY CREDIT LANDSCAPE



Source: StepStone Group, for illustrative purpose only.

These structural characteristics are reflected in the breadth and scale of the market opportunity. Estimates of the broader specialty credit universe vary, with some placing it at close to \$20 trillion globally, with further growth expected over time (Figure 2).¹

FIGURE 2: SPECIALTY CREDIT MARKET SIZE



Source: KKR, as of 2025, for illustrative purposes only.

These figures highlight that specialty credit is not a marginal niche, but an institutional-scale opportunity that remains relatively early in its adoption cycle.

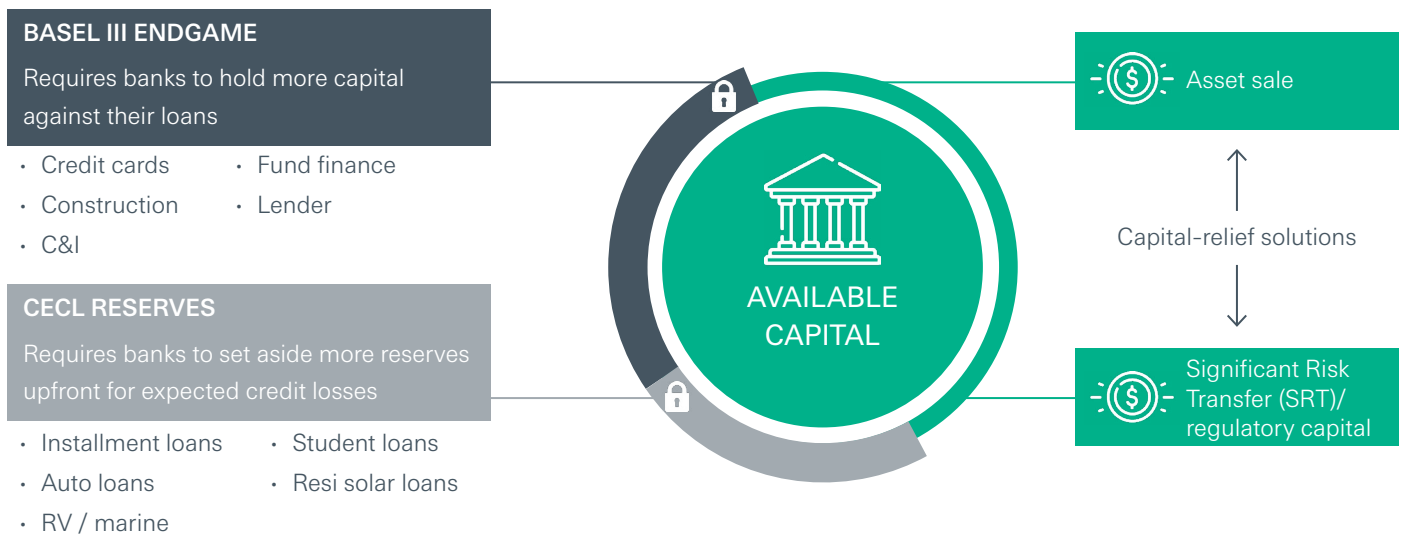
Why invest?

The investment case for specialty credit is supported by strong and growing demand for flexible financing solutions across sectors.

Many of the structural forces that drove the growth of modern direct lending are now reinforcing the expansion of specialty credit. Tighter banking regulation, higher capital requirements, and more burdensome accounting and provisioning standards have reduced banks' willingness and, in some cases, ability to hold certain assets and provide specialized financing. Regulatory developments, including the ongoing implementation of Basel III reforms and more stringent credit loss provisioning frameworks, have further contributed to this retrenchment (Figure 3). Periods of market dislocation often accelerate these dynamics further, as borrowers increasingly seek reliable and customized sources of capital.

For investors, this combination of rising borrowing demand and constrained traditional supply creates a particularly attractive environment, expanding the opportunity set while enhancing lenders' ability to negotiate favorable structures, pricing, and protections.

FIGURE 3: SPECIALTY CREDIT BENEFITTING FROM DISINTERMEDIATION



Source: StepStone Group, for illustrative purposes only.

¹ Apollo, 2023.

Role in a portfolio

From a portfolio construction perspective, specialty credit may complement both direct lending and public fixed income. Its exposures are often non-corporate, asset-based, and backed by large pools of collateral, reducing reliance on the financial performance of a single corporate borrower. Instead, repayments are anchored in contractual cash flows generated by underlying assets and reinforced by structural protections such as amortization, overcollateralization, covenants, and asset-level controls. As a result, specialty credit may be less sensitive to corporate earnings cycles and broader macroeconomic volatility.

Diversification

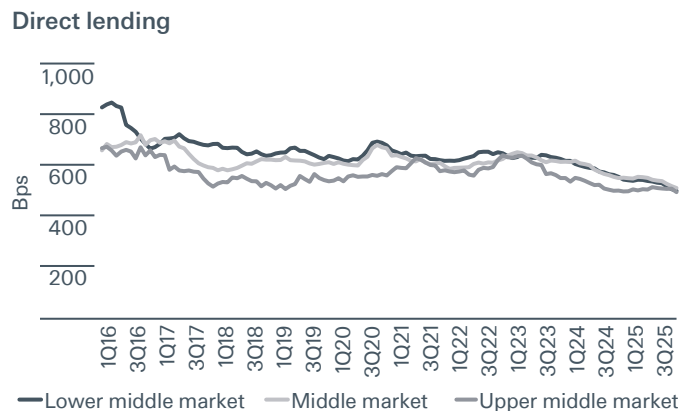
The diversification benefits are further strengthened by the breadth of underlying exposures. Asset classes such as consumer auto loans, aircraft leases, credit cards, royalties, and residential or commercial mortgages are driven by different economic factors and may therefore perform differently across cycles. Allocating across strategies, asset types, and geographies can improve portfolio robustness, particularly during periods of market stress.

Differentiated returns

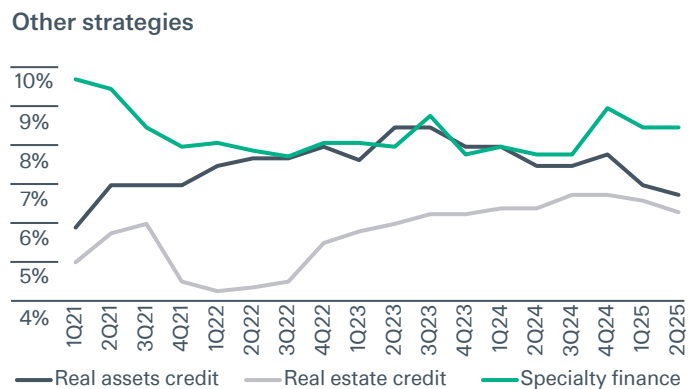
Specialty credit may also offer the potential for enhanced returns. The market is inherently complex and operationally intensive, requiring specialized expertise in asset-level underwriting, data analysis, servicing oversight, and legal structuring. These higher barriers to entry tend to limit competition and may support more attractive pricing and stronger structural protections. For investors, this complexity

may create a premium for skill, selectivity, and execution. In many cases, specialty credit strategies have the potential to generate incremental yield, often 200–300 basis points above comparable unlevered direct lending strategies, reflecting both the additional complexity and the differentiated nature of the underlying risks (**Figure 4**).

FIGURE 4: MEDIAN NEW ISSUE SPREAD



Source: Kroll StepStone Private Credit Benchmarks, as of November 2025. Note: Upper middle market refers to companies with EBITDA of \$75 million or greater; middle market refers to companies with EBITDA between \$25 million and \$75 million; and lower middle market refers to companies with EBITDA below \$25 million.



Source: Aksia DealVault, as of June 2025.

Building exposure

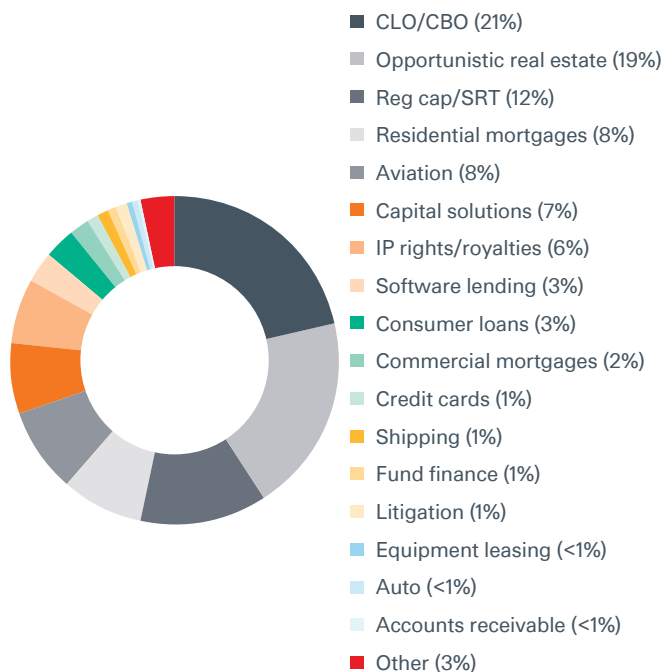
Building specialty credit exposure requires a deliberate focus on diversification across collateral types, sub-sectors, managers, and sourcing channels. Concentrating exposure in a single segment may limit the diversification benefits that specialty credit can provide (**Figure 5**). A well-constructed portfolio should therefore span hard assets, financial assets, and other specialty lending categories.

The diversity of the market also means that underwriting expertise is highly specialized. Aviation finance, for example, depends on lease structures, residual values and transportation markets, while consumer lending relies more heavily on borrower data, servicing capabilities, and repayment behavior. NAV lending introduces yet another set of counterparties, structures, and risk drivers. No single underwriting framework can be uniformly applied across the broader specialty credit universe.

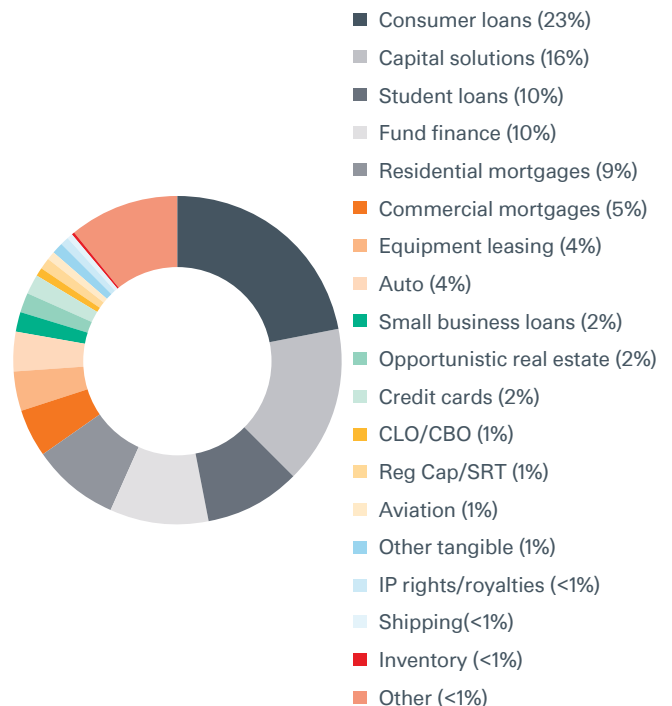
This specialization reinforces the importance of manager diversification. A multi-manager approach may broaden access to strong opportunities, specialized underwriting expertise, and diversified sourcing networks while reducing concentration risk. Diversified sourcing channels can further strengthen portfolio construction: Primary investments provide access to new deal flow, secondary transactions may accelerate deployment and reduce blind-pool risk, and co-investments can enhance portfolio economics through lower fees. Taken together, diversification across strategies, managers, and access channels is a key driver of portfolio resilience and long-term returns in specialty credit.

FIGURE 5: SPECIALTY CREDIT EXPOSURE BY COLLATERAL

VINTAGE I



VINTAGE II



Source: StepStone Group, as of December 2025.

Conclusion

Specialty credit represents a compelling evolution within private credit, expanding the opportunity set beyond traditional corporate lending and introducing strong returns. Its investment appeal is supported by three mutually reinforcing pillars:

1. Diversified collateral exposure

A well-constructed specialty credit portfolio spans a broad range of hard assets, financial assets, and niche lending strategies with distinct risk and cash flow drivers. This breadth of exposure may reduce reliance on any single sector, borrower, or economic factor, enhancing resilience across market environments.

2. Manager diversification

A multi-manager approach can broaden access to differentiated opportunities, specialized underwriting expertise, and diversified sourcing networks while reducing concentration risk.

3. Multi-channel access

Primary investments, secondaries, and co-investments each play complementary roles in portfolio construction. Combining these channels may improve deployment flexibility, increase visibility into underlying exposures, and enhance overall portfolio efficiency.

In an environment characterized by rising financing demand, continued bank retrenchment, and an increasing premium on specialized underwriting capabilities, specialty credit may offer investors enhanced diversification, access to attractive risk-adjusted returns, and more resilient credit portfolios.

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All data is as of May 2026 unless otherwise noted.

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