

KKR Credit

March Market in Review

As of March 31, 2022

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Market Overview

March 2022 KKR Credit Market Commentary

Observations

- A hawkish Fed narrative and a developing conflict in Ukraine produced sharply higher rates in March, a spike in commodity prices, and lower and then eventually higher prices for high-yield bonds and loans. March also produced the 2nd most significant spread tightening of the last 15 months, negligible new-issue volume, and an eventual stalling of 1Q22's most significant stretch of retail outflows on record (1Q -\$25.3bn). 2 and 10yr US Treasury yields rose 90bp and 52bp apiece in March and the 2s/10s curve briefly inverted for the first time since August 2019. High-yield bond yields rose 32bp and spreads tightened 40bp in March to 6.31% and 399bp, which are now 42bp and 72bp below March 15th's high
- Leveraged loans managed to produce modest gains in March (+0.11%) and significantly outperformed the balance of fixed income as a hawkish Fed and geopolitical tensions produced a sharp recalibration of interest rate expectations. The loan product also experienced lighter issuance, a reacceleration of retail inflows, an improvement in CLO activity (\$11.7bn ex-refi/resets), and a significant two-week rally (+1.89% 3/15-3/31) after seeing prices slide between late January and mid-March. Meanwhile loan yields (3yr) and spreads (3yr) rose 97bp and 8bp in March to 7.04% and 447bp amid geopolitical tensions and inflation induced 91bp spike in the 3yr forward curve
- As a fundamental-focused credit manager with deep resources to analyze credits, we are open to examining companies that the market may be shunning, and we believe from our analysis that there has been an indiscriminate rally in up-markets and a "flight to quality" in down-markets
- We continue to look at credit opportunities through a critical fundamental lens and feel well positioned to take advantage of continued volatility and spread dispersion as we still see dislocated situations that can offer strong risk adjusted return potential

Source: JP Morgan Monthly Research as of March 31, 2022.

Note: Unless indicated, the above reflects the current market views, opinions and expectations of KKR Credit based on its historical experience.

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March 2022 Market In Review

U.S. Markets ⁽¹⁾

Market Returns

- Bank loans and high-yield bonds returned -0.01% and -4.15% year to date, respectively, compared to returns for 10-year Treasuries of -6.82% and high-grade bonds of -7.69%

Issuance

- Gross high yield primary market activity remained low in March following 23-month low in February, amid heightened geopolitical concerns and interest rate volatility. Overall, only 18 bonds priced for \$9.9bn, which followed \$9.3bn on new volume in February
- Amidst heightened volatility across the broader markets, loan primary market activity decreased to a 20-month low in March, as \$21.6bn of gross loan volume priced over the course of month. This followed February's issuance of \$48.0bn, and volumes of \$50.9bn, \$27.6bn, and \$74.8bn in January, December, and November, respectively

Retail Flows

- High yield mutual funds outflows decreased in March, but it was still a third consecutive and fourth out of the last five months that the asset class has seen heavy outflows. Notably, March's outflow totaled -\$4.9bn, which followed a -\$9.6bn outflow in February, a 23-month-high -\$10.8bn outflow in January, a +\$4.2bn inflow in December, and a -\$5.0bn outflow in November. ETFs accounted for -\$2.4bn of outflows in March (vs -\$4.6bn in February), while actively managed funds reported a -\$2.5bn outflow
- Loan funds saw a 16th consecutive inflow in March, which totals a cumulative +\$65.6bn. Specifically, March's inflow totaled +\$2.2bn (+\$632mn ETF and +\$1.5bn actively managed), which was the lowest since Dec-2020, follows inflows of +\$6.9bn and +\$9.6bn in February and January (the 5th largest and largest inflows on record), and compares with an average monthly inflow of +\$4.1bn over the 16-month stretch of inflows (Dec20-Mar22)

CLOs

- New US CLO volume decreased in March after February's rebounded. Specifically, gross US CLO volume totaled \$13.3bn (\$11.7bn ex-refinancing and \$1.6bn refinancing) across 27 deals, compared with CLO issuance of \$28.2bn in February. Historically, March ranked six in terms of average monthly volume relative to the year's 12 calendar months. Specifically, March volume has averaged \$16.5bn since 2012; issuance in March 2021 totaled \$47.9bn

European Markets ⁽²⁾

Market Returns ⁽³⁾

- The European Leveraged Loan index returned +0.09% during the month. The European HY index returned -0.12% during the month

Issuance

- The European primary market issued €0.4bn of loans and €0.0bn of new bonds during the month of March

CLOs

- There were 11 new CLOs in Europe in March (€4.7bn). For YTD 2022, European CLO issuance was €9.8bn (across 23 deals)

March 2022 Market In Review

Originated Credit Markets ⁽¹⁾⁽²⁾

U.S. Markets

- **Direct Lending:** 2021 was a record year for deal activity and demonstrated the sustained, high demand for private debt financing. The direct lending market saw several tailwinds, including private equity dry powder hovering near its highs, robust levels of M&A and recapitalization activity, and a continued pivot away from banks toward private credit by borrowers. The strong momentum has continued into Q1 2022, albeit at a more tempered pace versus this time last year. We believe appetite for direct lending will remain strong particularly as the asset class has demonstrated resilience across market scenarios and provides an attractive yield premium. We continue to lean into partnerships with larger borrowers as we believe this area of the market provides an attractive risk-adjusted return. One of the major recent trends that we are seeing is the rise of mega-sized unitranche deals. There are an increasing number of opportunities in the market to deploy investor capital into \$1 billion-plus transactions. We view this size also as a validation of the private credit value proposition, as sponsors are electing to use a private solution in a segment of the market that where they historically would have used syndicated markets. Lastly, direct lending is well positioned to perform in a rising rate environment, given the fully floating rate nature of the underlying loans
- **Asset-Based Finance (ABF):** Our outlook for ABF is bright. We expect a continued rebound in the global demand for credit as economies emerge from the worst of the pandemic shutdowns. Further, we believe there will be continued bank retrenchment from ABF lending as banks' attention turns toward (i) addressing growing non-performing loans (which expands the NPL opportunity set) and (ii) compliance with financial regulations (e.g., Basel IV). At the same time, banks should continue to be willing providers of senior financing against ABF portfolios resulting in attractive returns. We also view the volatility in 2020 as reinforcing the benefits to banks and loan originators of working with larger, more established players, given the stability exhibited during 2021. Longer term, the asset class should benefit from the broader Private Credit themes such as the growth of global Millennial consumers and FinTech-enabled credit products to meet their needs

Restructuring / Distressed Markets ⁽²⁾

- Despite an increase in volatility and a sell off across the high-yield and leveraged loan markets, default activity remained a non-factor once again in March. Specifically, there was one default (Ruby Pipeline) totaling \$475mn in bonds and one distressed exchange (Sinclair's Diamond Sports Group) totaling \$6.3bn in bonds and loans in March. Notably, this marked the 17th consecutive month of three or fewer default actions, albeit it was the largest volume of debt affected over that span; default/distressed exchange volume averaged \$1.3bn per month over that span, ranging from \$200mn to \$3.9bn. March's one default and one distressed transaction followed one default and one distressed exchange totaling \$1.7bn in February and no defaults and one distressed transaction totaling \$240mn in January. In the first-quarter (YTD), a total of two companies defaulted totaling \$1.6bn in bonds and three companies completed a distressed exchange totaling \$7.1bn in bonds and loans. Notably 1Q22's \$1.6bn of actual defaults was the third lowest quarterly total since \$1.1bn defaulted in 4Q13, ahead of only 3Q21's \$855mn and 2Q18's \$1.5bn. Meanwhile, the combined \$8.6bn of default/distressed actions in 1Q22 driven primarily by Diamond Sport's distressed exchange was the highest quarterly default total since \$16.7bn defaulted in 4Q20. In 2021, default/distressed volume totaled \$3.4bn during the first quarter, \$5.1bn in 2Q, \$1.3bn in 3Q, and \$4.1bn in 4Q, or a quarterly average of \$3.5bn, compared with quarterly averages of \$35.4bn in 2020, \$14.8bn in 2019, and \$10.8bn in 2018. The par-weighted default rates for high-yield bonds and loans were 0.23% and 0.39%, respectively
- In European Markets, for the twelve months ended March 2022, the S&P ELLI default rate stood at 0.8%, which is ~120bps less than the March 2021 LTM default rate of 2.0%

(1) Source: KKR Credit Analysis as of March 31, 2022.

(2) Source: JP Morgan Monthly Research as of March 31, 2022, and S&P (ELLI) as of March 31, 2022.

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The current market views, opinions and expectations of KKR Credit based on its historical experience.

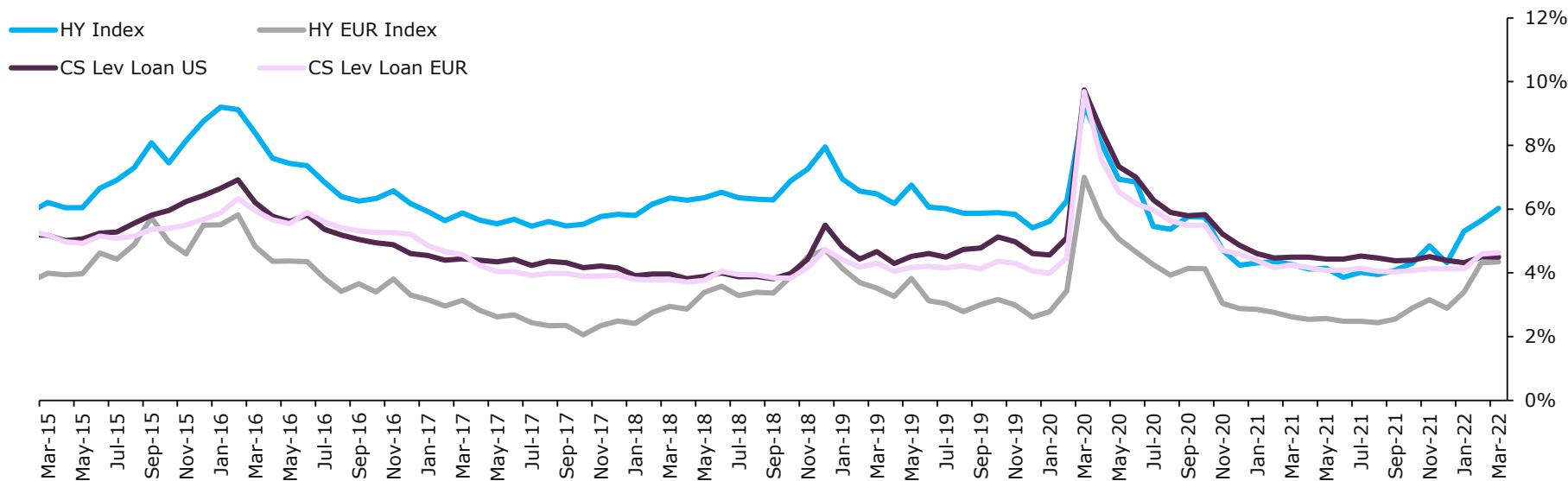
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Bank Loan and High-Yield Performance

	Yield to Worst (Bp)				Option Adjusted Spread (Bp)				Total Return		
BAML Indices	Mar-22	Feb-22	Mar-21	Mar-20	Mar-22	Feb-22	Mar-21	Mar-20	MTD	YTD	1 Year
US High Yield Master II	603	564	427	924	343	377	336	877	-0.93%	-4.51%	-0.29%
US High Yield BB	498	463	347	692	237	275	244	641	-1.18%	-5.37%	-0.87%
US High Yield B	638	598	451	1001	377	411	369	957	-0.54%	-3.46%	+0.07%
US High Yield C	982	950	718	1835	729	771	656	1794	-0.98%	-3.72%	+1.05%
Euro High Yield	435	432	262	700	400	445	314	754	-0.12%	-4.83%	-3.14%

	Discount Margin (3 years) (Bp)				Spread (Bp)				Total Return		
	Mar-22	Feb-22	Mar-21	Mar-20	Mar-22	Feb-22	Mar-21	Mar-20	MTD	YTD	1 year
CS US Lev Loans	L+449	L+450	L+449	L+974	363	363	356	349	+0.04%	-0.10%	+3.22%
CS EUR Lev Loans ⁽¹⁾	E+463	E+459	E+425	E+968	369	367	361	350	+0.09%	-0.53%	+2.31%

Historical Loan and Bond Yields / Discount Margins (%)



(1) Credit Suisse European Leveraged Loan Index returns presented are hedged to Euro.

Source: BAML Market, S&P LCD Comps, and Credit Suisse as of March 31, 2022.

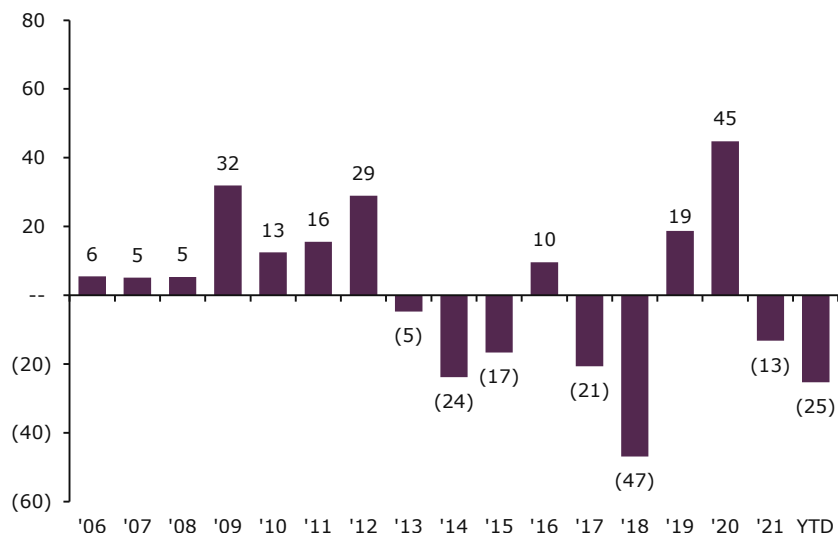
Mutual Fund Flows

U.S. Markets

- **High-Yield:** High yield mutual funds outflows decreased in March, but it was still a third consecutive and fourth out of the last five months that the asset class has seen heavy outflows. Notably, March's outflow totaled -\$4.9bn, which followed a -\$9.6bn outflow in February, a 23-month-high -\$10.8bn outflow in January, a +\$4.2bn inflow in December, and a -\$5.0bn outflow in November. ETFs accounted for -\$2.4bn of outflows in March (vs -\$4.6bn in February), while actively managed funds reported a -\$2.5bn outflow
- **Bank Loans:** Loan funds saw a 16th consecutive inflow in March, which totals a cumulative +\$65.6bn. Specifically, March's inflow totaled +\$2.2bn (+\$632mn ETF and +\$1.5bn actively managed), which was the lowest since Dec-2020, follows inflows of +\$6.9bn and +\$9.6bn in February and January (the 5th largest and largest inflows on record), and compares with an average monthly inflow of +\$4.1bn over the 16-month stretch of inflows (Dec20-Mar22)

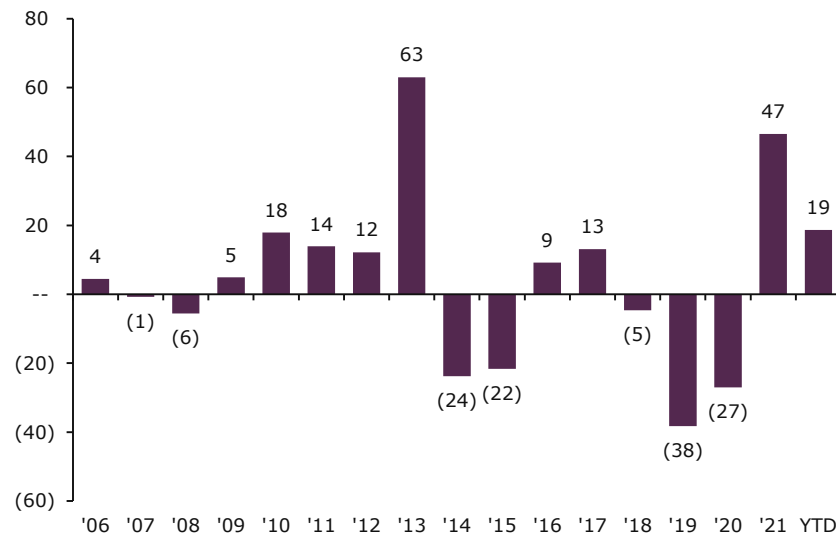
U.S. High-Yield Mutual Fund Flows

\$ Billions



U.S. Bank Loan Mutual Fund Flows

\$ Billions

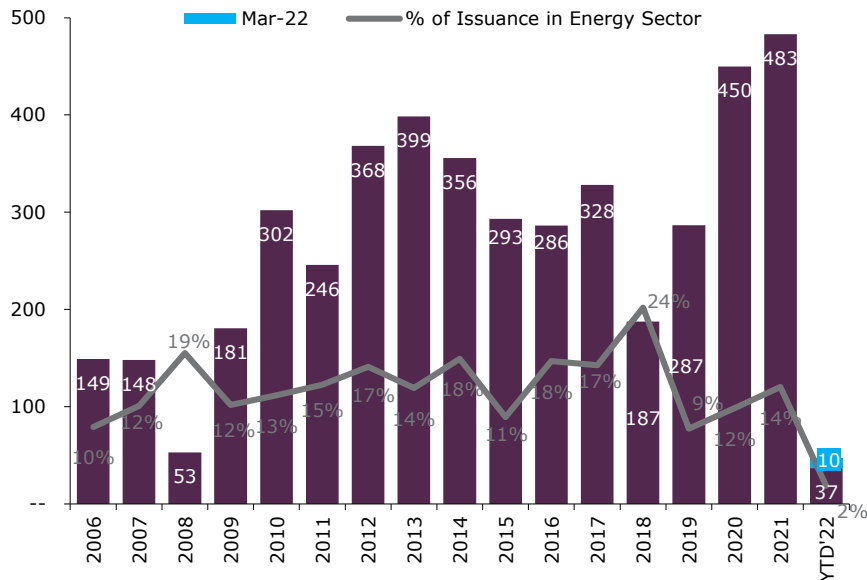


New Issuance – U.S.

- **High-Yield:** Gross high yield primary market activity remained low in March following 23-month low in February, amid heightened geopolitical concerns and interest rate volatility. Overall, only 18 bonds priced for \$9.9bn, which followed \$9.3bn on new volume in February
- **Bank Loans:** Amidst heightened volatility across the broader markets, loan primary market activity decreased to a 20-month low in March, as \$21.6bn of gross loan volume priced over the course of month. This followed February's issuance of \$48.0bn, and volumes of \$50.9bn, \$27.6bn, and \$74.8bn in January, December, and November, respectively
 - March loan volume has historically ranked as the third in terms of average monthly volume relative to the year's 12 calendar months

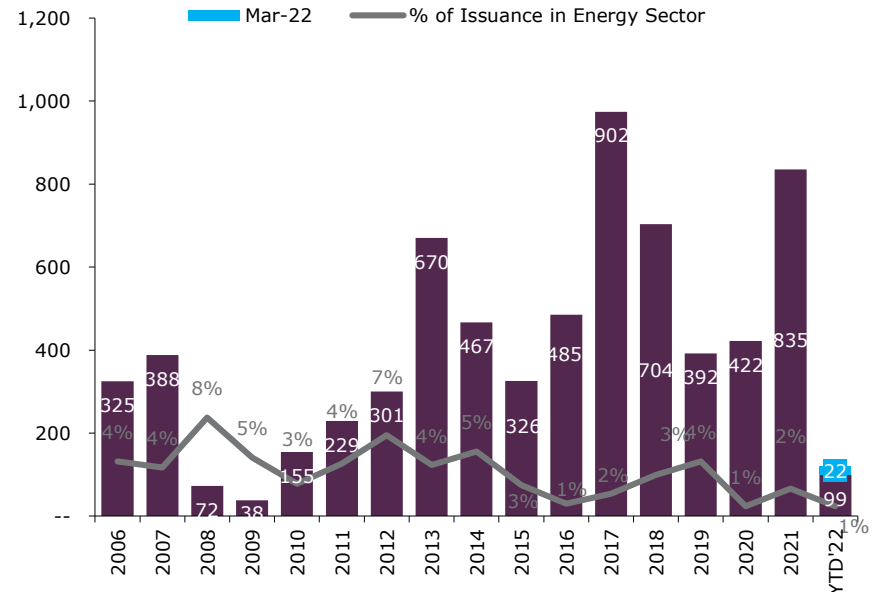
High-Yield Issuance

\$ Billions



Bank Loan Issuance

\$ Billions

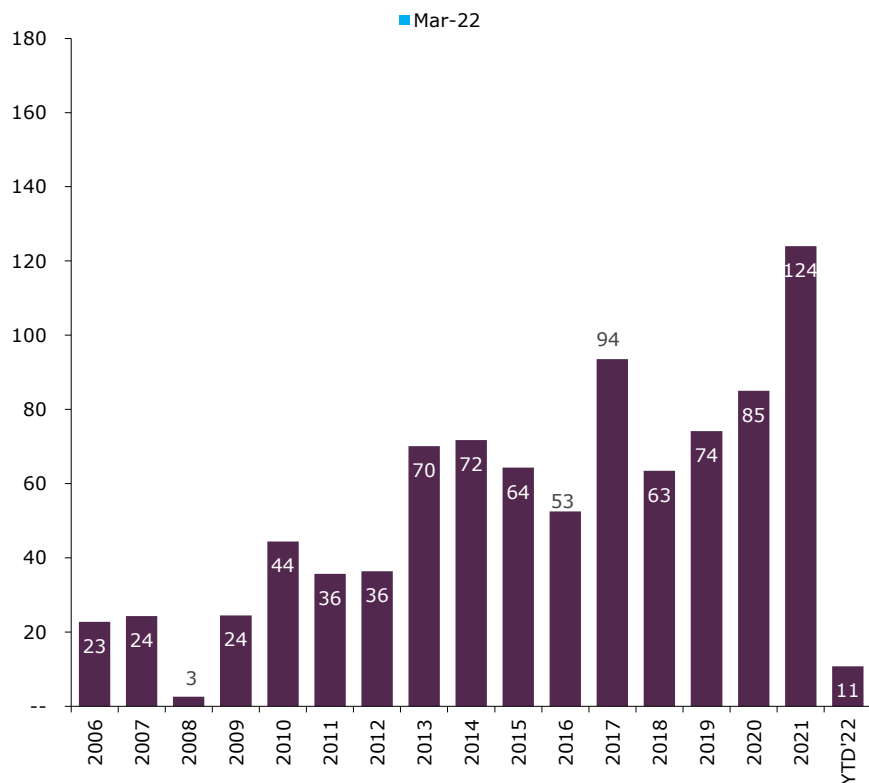


New Issuance – Europe

- **High-Yield:** €0.0 bn high-yield paper has been issued in March 2022
- **Bank Loans:** €0.4 bn of loan paper has been issued in March 2022

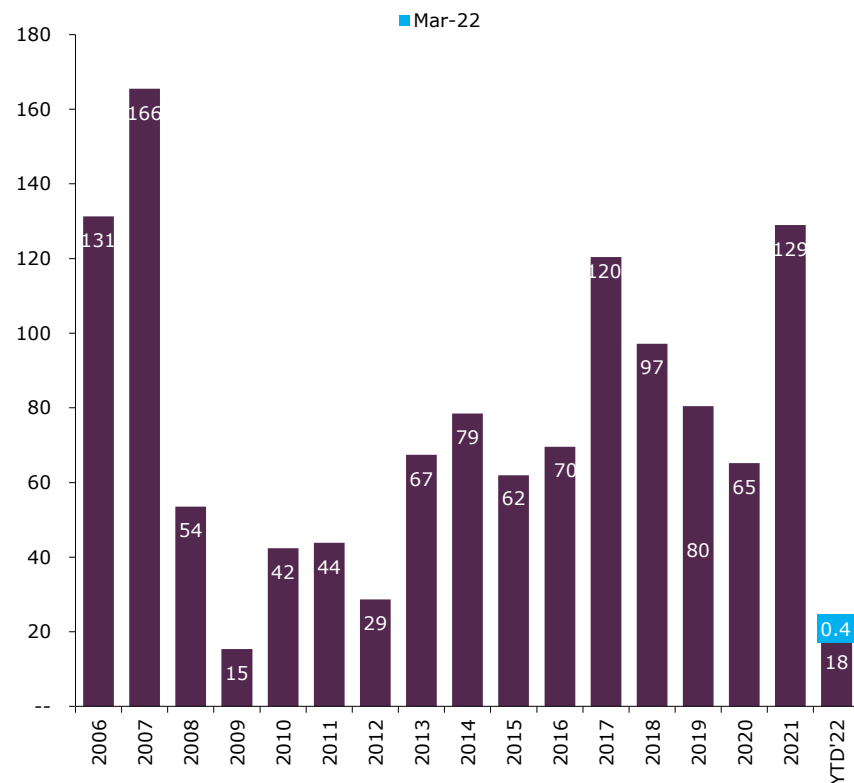
High-Yield Issuance

€ Billions



Bank Loan Issuance

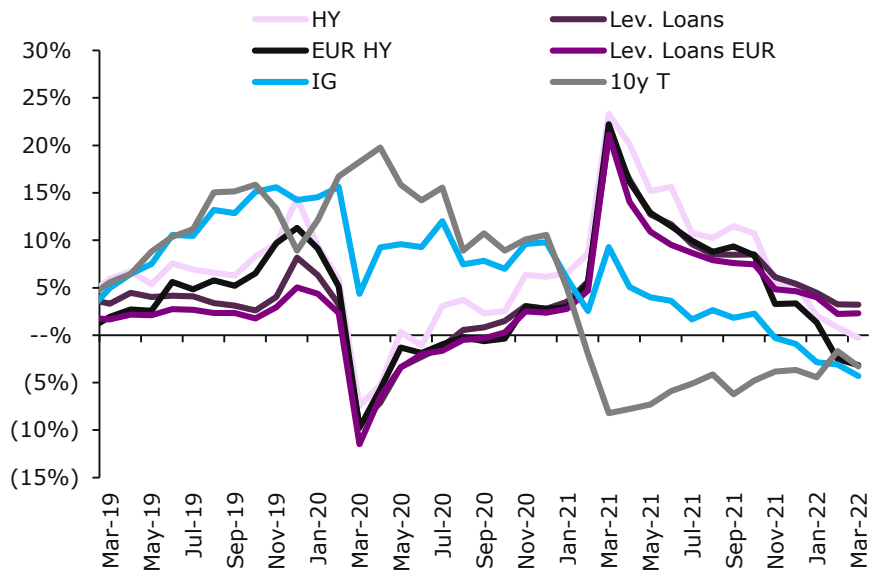
€ Billions



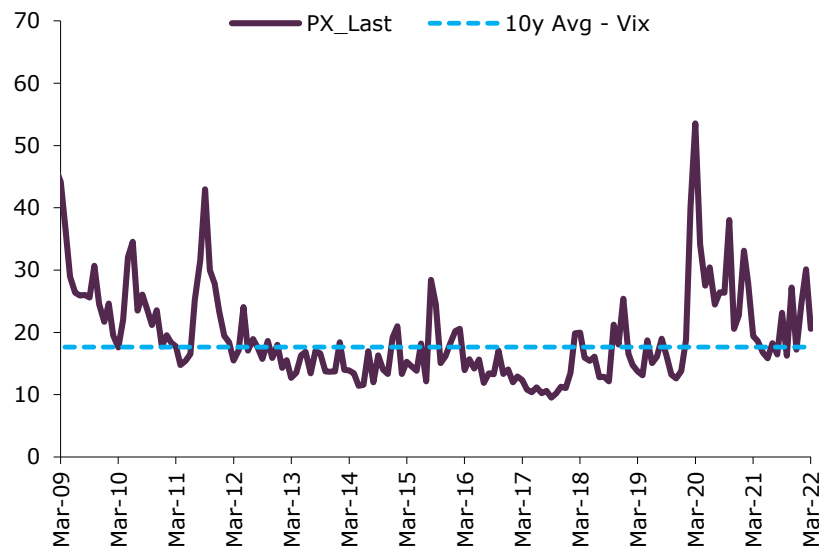
Returns and Volatility⁽¹⁾

- Bank loans and high-yield bonds returned -0.01% and -4.15% year to date, respectively, compared to returns for 10-year Treasuries of -6.82% and high-grade bonds of -7.69%
- The European Leveraged Loan index returned +0.09% during the month. The European HY index returned -0.12% during the month
- Over the past twelve months, high-yield bonds in the U.S. and Europe have provided cumulative returns of -0.29% and -3.14%, respectively. Bank loan performance has totaled +3.22% (U.S.) and +2.31% (Europe), while U.S. IG bonds have returned -4.31%. The twelve-month total return for the 10y Treasury was -3.31% at the end of the month
- High-yield bond yields increased ~39bps during the month; the yield on the BAML US HY Master II Index at the end of March was 603bps
- Volatility decreased in March with the VIX at 20.6, from February's 30.2

Cumulative 1y Total Returns (%)

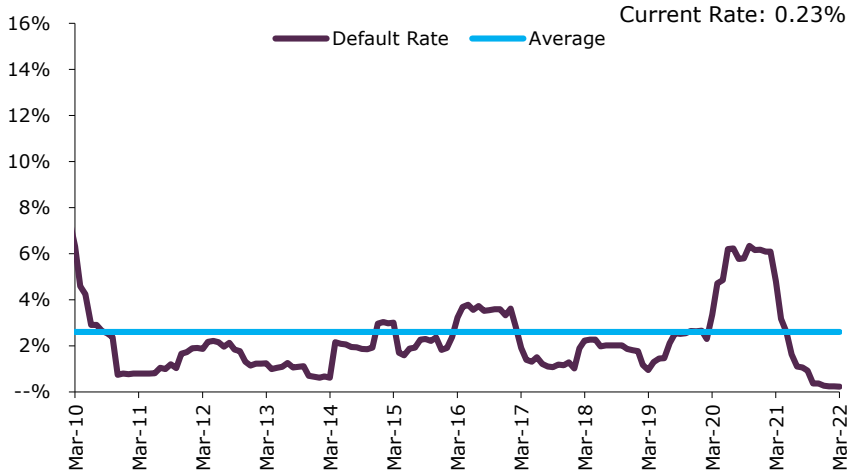


Volatility

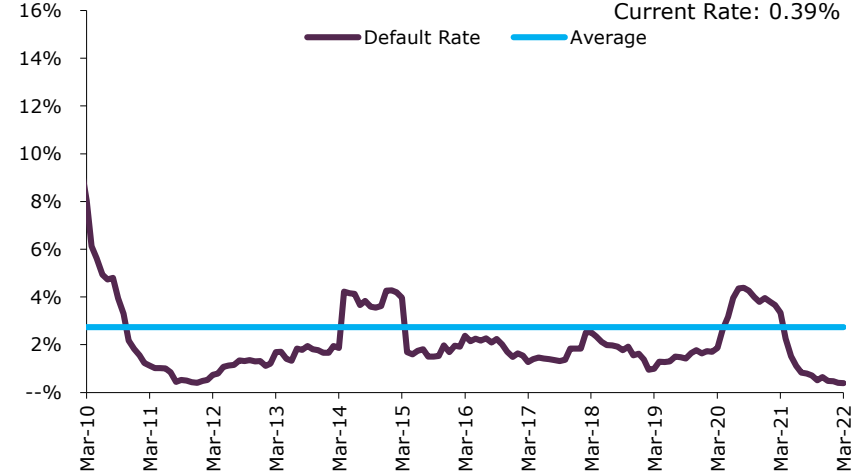


Default and Recovery Rates – U.S.

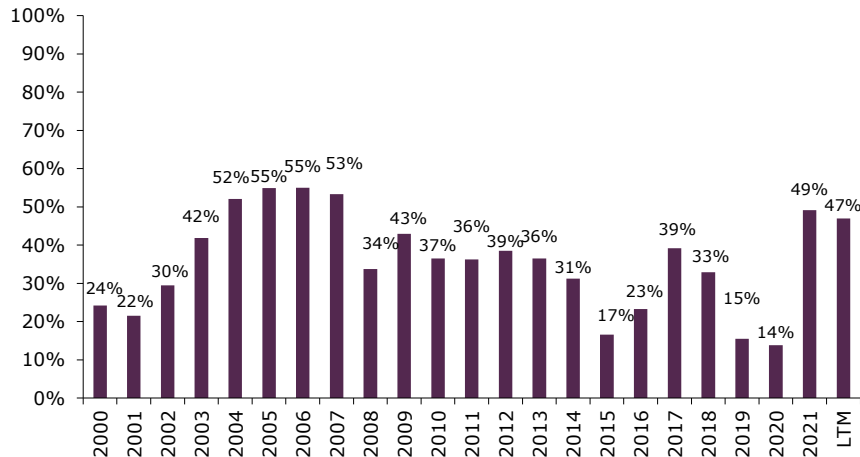
LTM High-Yield Default Rate (%)



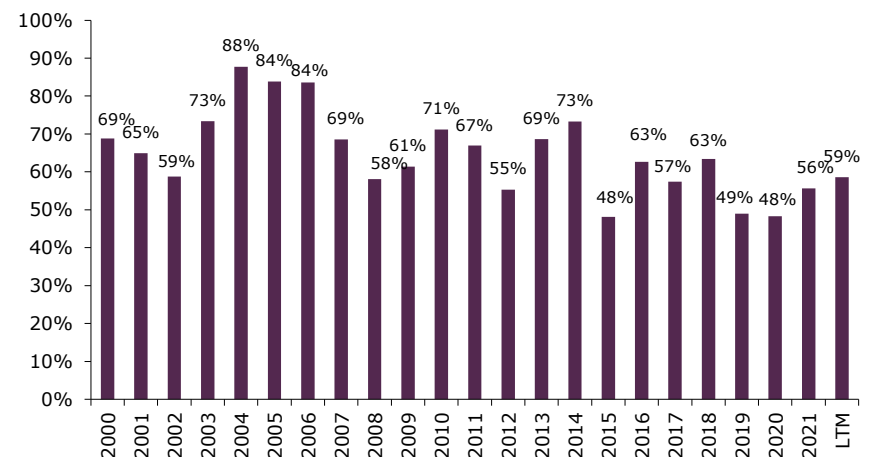
LTM 1st Lien Default Rate (%)



LTM High-Yield Recovery Rate (%)



LTM 1st Lien Recovery Rate (%)



March 2022 Largest New Issues

Top Bank Loan Issuers

Launch Date	Issuer Name	Country	Industry	Purpose	S&P CCR	Moody's CCR	Deal Size	RC Amount	TLA	TLB	TLC	TLD	Cov-Lite	Sponsor
03/21/22	Novolex	US	Chemicals	M&A/LBO	B	B3	3,000			\$3000M / SOFR+425			Yes	Apollo Management
03/21/22	Novolex	US	Chemicals	M&A/LBO	B	B3	500	500					No	Apollo Management
03/11/22	Owens-Illinois	US	Building Materials	Corp Purpose	B+	B1	2,800	1250		\$500M / SOFR+150			No	Not Sponsored
03/04/22	Iron Mountain Inc	US	Services & Leasing	Refinancing	BB-	Ba3	2,750	2500		\$250M / SOFR+175			No	Not Sponsored
03/28/22	Perrigo Co	US	Healthcare	M&A / Acquisition	BB-	Ba1	800			\$400M / SOFR+275 - 300			Yes	Not Sponsored
03/28/22	Perrigo Co	US	Healthcare	M&A / Acquisition	BB-	Ba1	1,300	1000	\$300M / NA				No	Not Sponsored
03/08/22	SPX Flow	US	Manufacturing & Machinery	M&A/LBO	B-	B3	1,610			\$1610M / SOFR+450			Yes	Lone Star Funds
03/08/22	SPX Flow	US	Manufacturing & Machinery	M&A/LBO	B-	B3	200	200					No	Lone Star Funds
03/22/22	Houghton Mifflin Harcourt Publishing Co	US	Printing & Publishing	M&A/LBO	B	B3	1,480			\$1480M / SOFR+500 - 525			Yes	Veritas Capital
03/22/22	Houghton Mifflin Harcourt Publishing Co	US	Printing & Publishing	M&A/LBO	B	B3	250	250					No	Veritas Capital
03/23/22	SS&C Technologies	US	Computers & Electronics	M&A / Acquisition	BB	Ba3	650			\$650M / SOFR+225			Yes	Not Sponsored
03/23/22	SS&C Technologies	US	Computers & Electronics	M&A / Acquisition	BB	Ba3	880			\$880M / SOFR+225			Yes	Not Sponsored
03/10/22	Owens & Minor Inc	US	Healthcare	M&A / Acquisition	BB-	Ba3	600			\$600M / SOFR+375			No	Not Sponsored
03/10/22	Owens & Minor Inc	US	Healthcare	M&A / Acquisition	BB-	Ba3	150	150					No	Not Sponsored
03/23/22	Owens & Minor Inc	US	Healthcare	M&A / Acquisition	BB-	Ba3	500		\$500M / NA				No	Not Sponsored
03/09/22	Restaurant Technologies	US	Food & Beverage	M&A/LBO	B	NR	810			\$810M / SOFR+425			Yes	Energy Capital Partners
03/09/22	Restaurant Technologies	US	Food & Beverage	M&A/LBO	B	B2	100	100					No	Energy Capital Partners
03/28/22	Doosan Infracore	KOR	Manufacturing & Machinery	Refinancing	BB	Ba3	850			\$850M / SOFR+275 - 300			Yes	Not Sponsored

March 2022 Largest New Issues

Top High Yield Issuers

Settle Date	Issuer Name	Country	Industry	Purpose	S&P Bond Rating	Moody's Bond Rating	Size	Issue	Yield	Years
03/28/22	Ford Motor Credit Co	US	Services & Leasing	Refinancing	BB+	Ba2	1,500	Senior Notes	4.950%	5
03/10/22	Macy's Inc	US	Retail	Refinancing	BB	Ba2	425	Senior Notes	5.875%	8
03/10/22	BellRing Brands	US	Food & Beverage	M&A/Spinoff	B	B3	840	Senior Notes	7.000%	8
03/29/22	Owens & Minor Inc	US	Healthcare	M&A/Acquisition	B	B2	600	Senior Notes	6.625%	8
03/17/22	Crown Holdings Inc	US	Metals & Mining	Corp Purpose	BB-	Ba3	500	Senior Notes	5.250%	8
03/08/22	Energizer Holdings Inc	US	Computers & Electronics	Refinancing	B	B2	300	Senior Notes	6.500%	5.75
03/16/22	Carpenter Technology	US	Metals & Mining	Refinancing	BB+	B2	300	Senior Notes	7.625%	8
03/08/22	LSB Industries Inc	US	Chemicals	M&A/Acquisition	B	B2	200	Add-on Secured	6.250%	6.5
03/17/22	Guitar Center Inc	US	Retail	Refinancing	B	B3	200	Senior Notes	8.330%	3.75
03/31/22	Presidio	US	Computers & Electronics	Corp Purpose	CCC+	Caa1	125	Add-on Senior	8.467%	6
03/31/22	Presidio	US	Computers & Electronics	Corp Purpose	CCC+	Caa1	25	Add-on Senior	8.028%	6