

CADC: A CONVERSATION WITH  
THE PORTFOLIO MANAGER

# PLAYING DEFENSE AND OFFENSE IN THE CURRENT ENVIRONMENT

Mitch Goldstein, Partner of Ares and Co-Head of Ares Credit Group, recently sat down with Derek Schwartz, Head of Strategic Accounts at CION Investments, for a discussion about the current market environment and where the risks and opportunities may be.

They discussed recent headlines about the asset class and how the portfolio managers have positioned the fund in the ten years since inception, which have encompassed global dislocations, market downturns, several different interest rate regimes, and multiple administrations.

The full conversation is below.

## MITCH GOLDSTEIN

There has never been as much press on this asset class as we've seen in the last six to eight months. We were investing through the global financial crisis and the pandemic. We've had supply chain issues, inflationary issues, macro recessions, whether they're metals and mining or the Amazon effect on retail. We've had high interest rates and low interest rates over the last 20 years

of investing at Ares. We've had five administrations and eight different leadership changes in the UK. There's always a question of the day. In the fall, the question of the day was Tricolor and First Brands. And while that was not direct lending in any way, shape, or form, the press, every article, the headline was direct lending and then talking about Tricolor and First Brands.

Now the question of day is software and AI. To take a step back and look at what the fund looks like today, the first thing I'd like to point out is how diversified it is, with just under a thousand issuers as of December 31, 2025. We see software and software related services as a leading industry, but no one company in that industry group is material.

Overall, we are seeing interest coverage decrease and leverage has come down in the last few years. As of year-end, non-accruals were at a historically low average over the 20 plus years at Ares, however non-accruals don't necessarily mean ultimate credit losses.

Ares has a long history, even on non-accruals, of getting their money back. There is nothing that we're seeing in the numbers that would suggest anything that the press is writing about. We see these as fundamentally healthy companies, and this is a fundamentally diverse, healthy portfolio.

Every deal we participate in goes in at Original Issued Discount (OID), and eventually we amortize it to par. These companies are quite large, substantial companies with lots of equity below us.

Is AI going to take market share away from these software companies? We've been investing in software for well over a decade and to date have experienced success in our software investments. Our diligence is focused on technology risk and obsolescence. AI is not new to Ares; we have a team of people that do nothing but underwrite and invest in software. AI does an exceptional job at taking lots of data, synthesizing it and coming up with conclusions. We don't invest in companies that do data analytics. At the very high end, content creation is something that AI does really well. We don't invest in software companies that do content creation. What are the types of software companies that we invest in? They tend to be Enterprise Resource Planning (ERP) systems that are embedded in the workflow or the organizational processes of a company, which is software that keeps track or controls your inventory or your receivables, or your communication with your clients. It is software that takes proprietary information only known to that company and allows management to understand what's going on in that company. These are workflow types of businesses that guide how one project leads to the next. We are seeing the software companies in our portfolio continue to grow, continue to generate cash, continue to add customers and their renewals.

In short, we are not experiencing what you're reading in the press as a credit matter. We're seeing continued growth in our software book. Our goal is to make money for our investors in a number of different ways. We make our loans and we get an upfront fee. We take that upfront fee and amortize it over several years to get an all-in yield. Our loans tend to last two to two and a half years. Historically, I think it's right around 2.3 years. As base rates have come way down in this interest declining environment, our all-in yields have come down too.

In the last couple of quarters in 2025, we were right around historical average in terms of risk-adjusted return or yield per unit of leverage.

When credit is in a benign era, we tend to charge less for credit. When there's more volatility, we can charge more. For example, due to the increased volatility in 2023, we charged more. In the volatility in the last couple weeks, our spreads have increased in a very short period of time. As you would expect in periods of volatility, like we're experiencing now, Ares is seeking to take advantage of better pricing and fees on our loans.

When there are periods of volatility, Ares has historically outperformed. This is a period of volatility and we're seeing some really nice investment opportunities, but that is not new to us. In our experience, direct lending tends to outperform other credit products, whether it's syndicated loans or high yield bonds. It's what we call downside mitigation. I talked about diversity, loan-to-value, senior secured, and the first lien nature of this portfolio.

Our goal is to find the best risk-adjusted return in the credit markets globally and take advantage of the volatility.

## **DEREK SCHWARTZ**

**The NAV in the fund since post-Liberation Day has been soft. What are some of the reasons for the softness in the NAV between last October through the first part of this year?**

## MITCH GOLDSTEIN

This fund is 20% liquid loans, and then there's Collateralized Loan Obligation (CLO) debt and equity, which is liquid. The leveraged loan market had a lot of volatility at the end of last year and at the beginning of this year. Those are unrealized losses. If a loan trades from par to 95, that's going to affect the NAV. In April 2025, on Liberation Day, the NAV ticked down, and then we had to earn our way back. That 20 to 25% of the fund that we keep liquid for redemptions will have a little more volatility than the direct lending part.

In our CLO equity, our traders buy equity and debt. And over the last couple months, we actually have trimmed our Bulge Bracket (BB) exposure. I think we traded \$10 million to \$20 million off of that, all above par that resulted in NAV accretion. Our traders look to take advantage of what they see in the market. You will see some NAV movements up and down because of that liquid loan portfolio. But over time, I think we were able to drive better value by dynamically rotating to try to take advantage of that volatility, while working to generate a consistent premium to other asset classes.

## DEREK SCHWARTZ

In essence, you're exchanging a little bit of NAV volatility today for potential returns down the road.

## MITCH GOLDSTEIN

CLO equity, which had some volatility, has seen some attractive yields and has been accretive. We're willing to withstand a little volatility for potential attractive yields on that CLO equity.

## DEREK SCHWARTZ

We have won mandates with pension funds who like this structure with the liquidity bucket even though it does add a little bit of NAV volatility. When you talk to your institutional clients, what do you think those investors are focused on right now that gives them confidence to continue to allocate capital?

## MITCH GOLDSTEIN

Most of the institutional investors are asking, how can we take advantage of this market? These are long-term investors. What's amazing about the direct lending market is that interval funds and the private BDC sector are relatively new. Public BDCs have been around for a long time but the growth in the retail market is fairly new. Institutional investors have been invested in this market for 20 to 30 years. The institutional investors who have been doing this for a long time understand the ups and downs of the market. They have come to appreciate that over time, this asset class has the ability to outperform other asset classes. We saw what Blue Owl did. They sold a number of their assets to institutional investors who were more than happy to take these loans. And in periods of volatility, that's what the institutional investor does. They look for opportunities to give them an advantage. We are working with a number of institutions now to find ways to take advantage, which is what we tend to do during periods of volatility.

## DEREK SCHWARTZ

Mitch, so much attention is being put on private credit through the media, especially as it relates to software, but it doesn't seem to be as much as it relates to the private equity side of things. How do you folks at Ares think about that? There seems to be a lot of equity cushion but there doesn't seem to be a lot of talk about the risk on the equity side. Is that something that you folks look at, and how do you view that?

## MITCH GOLDSTEIN

Private equity and private debt are inextricably linked. One asset class needs the other asset class to thrive. We want the private equity firms to do well, we want them to buy companies, grow the companies, sell the companies, and obviously

borrow money all along the way. We like private equity during periods of volatility. If the company is not working and needs a little more liquidity a large institution writes a check to help that company out. That has been our experience, during COVID and over the last 20 years.

Private equity will typically write a check because they don't want to give up the company at 40 cents on the dollar. It has been our experience when we invest in good quality companies, we have seen growth. The goal is to support these companies if they hit a road bump. We find it odd that private debt is singled out in the press. The private equity guys will have a little more work to do and they'll do that. They have a history of generating nice returns, but as they generate those returns, we have the potential to earn income along the way, even during these periods of volatility.

## **DEREK SCHWARTZ**

**Shifting gears a little bit, there's clearly consternation around liquidity and private credit. Could you talk about the liquidity? How do you establish a structure where you're comfortable being able to do what you want to do as a manager, as well as provide liquidity so that investors have access to their capital? Are you doing anything different in light of the turbulence in the market?**

## **MITCH GOLDSTEIN**

We're going to run the fund in a manner that allows us to provide liquidity. Approximately 20% of the fund is liquid loans. We can sell those on almost any given day. We have leverage facilities. We don't run this fund with maximum leverage. Our loans tend to last two and a half years, so there's a natural runoff. Our direct lending loans and even our liquid loans have quarterly amortizations. Now, it's not a lot, but quarterly they pay back their loans. There are a number of different avenues where we can create liquidity.

## **DEREK SCHWARTZ**

**There's obviously been a lot of questions around PIK, payment-in-kind. Are you seeing it trend higher?**

## **MITCH GOLDSTEIN**

The press talked about it a lot last year. I don't think you will hear about it a lot this year. There is PIK that we like, and then there's bad PIK. If a company is on non-accrual, that usually is PIK. There are often times when we invest in junior securities or preferred stock that we know we're going to get PIK. They're generally not cash-paying securities.

We make the investment because we like that relative value. They tend to be held three to six years, and they have the potential for good risk-adjusted returns. A lot is written about PIK, but not enough is written about where that PIK is coming from. The good PIK versus the PIK that you don't want to have happen.

## **DEREK SCHWARTZ**

**One of the questions is about whether Ares is allocating and taking even more opportunity to get into software. Can you speak to that and how you see that trend continuing?**

## **MITCH GOLDSTEIN**

Given the volatility in software, I don't think software M&A will be like it was the last couple years. I think software will, over the near term, decrease a little, not a lot, because there's not going to be a lot of churn in the portfolio. It'll amortize down and there'll be some leakage. I don't think the software book will grow. When there are periods of volatility, what we have seen in the past is that when leverage comes down, yields, pricing and returns tend to go up. We believe there are going to be great opportunities in software.

Our hope is that we can rotate, not increase our software exposure, but rotate into higher-yielding, lower-levered software over the next couple of months, as the banks probably won't underwrite software in this market. I don't think there'll be a lot of new opportunities. I think M&A and software will be put on hold until private equity firms can articulate the AI story and what's going on in their books.

## **DEREK SCHWARTZ**

**Maybe you could talk a little bit about how origination compares to previous years? How does that compare to your competitors?**

## **MITCH GOLDSTEIN**

What we have found is that during these periods of volatility, the companies and sponsors recognize that direct lending can be a consistent, reliable source of capital in good markets and bad. Even during COVID, we were active and found success with our sponsors.

A lot has been written about the money coming in; what hasn't been written is our market share gains over the last decade or so. And so, it's not uncommon today for us to be part of a five plus billion-dollar unitranche; a decade ago that would have gone to the leveraged loan and high yield market. We've definitely taken market share from those two markets, and we continue to grow our market share post-periods of volatility.

Our gross origination is \$70 to \$80 billion these days. Our "yes" ratio is less than 5%. We say "no" nine out of 10 times. What I find so amazing from my seat is when you reverse engineer the numbers, you can get a sense of our origination machine and how much deal flow and information actually flows through the Ares offices around the globe each and every year. We decide what we think are the best credits. Even during periods of volatility, when there are questions on interest rates, or tax regimes, or supply chains, and now questions on software, over a really long period of time, we have been able to perform as a matter of credit. Historically, we have been able to perform as a matter of premium to other credit asset classes.

## **DEREK SCHWARTZ**

**When Ares is underwriting these deals, you're holding these loans across your different clients. You're not syndicating these out. I know that's an old question that we've addressed over the years, but can you address the integrity and importance of your underwriting? Because you are long-term investors in these credits relative to how the syndicated loan market works.**

## **MITCH GOLDSTEIN**

We are not public company investors, which I think is an important distinction. We're getting access to information that public companies don't provide investors. The team at Ares is tearing apart financials, getting historical data and getting detailed projections, and comparing and contrasting. 50% of the origination are companies that have been part of the portfolio for a long time. There are many companies that we've been lending to for five or 10 years plus. We have experience anticipating how companies may perform in good and bad markets and how their management performs against budget. I sit on the board of a couple companies and during the busy season, I have access to daily sales reports.

You don't get that as public investors. We have more access to real-time information versus public company investors. We approach underwriting differently. As I said, half of our originations, are with companies we have invested in previously. And the other half, are companies we look to underwrite. When we underwrite a company; it's not like we're doing a week or two of work. There are many companies where it takes months. We're tearing apart financials, we're comparing, contrasting to competitors. We're challenging management. We're visiting them. We're getting third party reports, consultant reports, legal reports, and quality of earnings reports. The immense due diligence that we perform before we lend money to a company does not take days; it takes weeks and months, sometimes three to six months. It's

a very thorough and complex underwriting process. It is a private equity type of process where, by the time you lend, you know everything about a company. And again, as I talked about, 50% of the companies we lend to we've been lending for years, we understand these companies. Part and parcel, we have so much more information than a public company investor.

## DEREK SCHWARTZ

When you step back from the headlines, what gives you the highest conviction in the strategy over the next 12 to 24 months?

## MITCH GOLDSTEIN

It's the team, it's our underwriting, it's our ability to maneuver in good times and volatile times. We are maneuvering now, focused on how we can take advantage of these periods of volatility, to seek more yield and more fees. We take some comfort in the diversity of this fund. No one company, no one sponsor, no one geography, no one vintage actually matters. Our goal is to increase that diversity. As I said, there were 900 plus companies as of year-end, and we add companies every day or so. The premiums that we will continue to seek out versus other credit asset classes, whether it's investment-grade leveraged loans, high yield bonds, et cetera, that is our main goal. We have a lot of conviction in the credits that we've underwritten, in the team that's underwriting them, in the diversity and the durability of this asset class.

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CAD000377-1226

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