

Servicing the alpha:

Why loan servicing is where private credit returns are protected – or quietly lost

Unlock operational efficiency to expand margins and support scale

The alpha in private credit isn't only won at origination. It's protected – or quietly surrendered – every day after the loan closes.

That's not a comfortable truth for an industry that prizes its underwriting. But as spread compression tightens margins across the market and institutional LP scrutiny moves from the credit memo to the operations room, the firms that treat servicing as a back-office afterthought are carrying a risk they can't yet see on their P&L.

This article distills the core argument of our full white paper, "Servicing the alpha": that loan servicing is the most controllable source of margin and scale in direct lending, and that the decisions made in how you board, monitor and report on loans will define your operating economics as much as the terms you negotiate.

The compression problem isn't going away

Spread compression is no longer a cycle – it's a structural condition. According to a 2026 O'Connell Lending Insights survey of 200 commercial lending professionals, 95% of lenders report spread compression across their portfolios. Data from the Debtwire Private Credit Forum confirms the trend: the middle market spread premium to the upper middle market narrowed from 200 basis points in 2024 to 100 basis points in 2025. Unitranche transactions are now pricing around 475 basis points.

What that means operationally is stark. The yield cushion that once absorbed servicing inefficiency no longer exists at the same depth. Every basis point you leave on the table through manual processing, delayed lifecycle events or reconciliation drag is a basis point you can't recover through origination. At scale, that math compounds fast.

The firms that understand this have stopped treating servicing cost as a fixed overhead. They're treating it as a variable they can manage – and a source of differentiation they can build.

The servicing scaling tax

Most private credit operations have a hidden problem: servicing cost scales linearly with AUM. Every loan added to the portfolio adds roughly the same operational burden. More loans means more headcount, more manual steps and more reconciliation cycles. There's no operating leverage in that model.

We call this the servicing scaling tax. It's the cost imposed by origination-centric firms that never redesigned their back office to keep pace with their front office. As deal velocity increases and portfolio complexity grows across direct lending, unitranche and syndicated structures, the tax compounds.

The firms breaking this pattern share a common characteristic: they've invested in servicing infrastructure that decouples cost growth from AUM growth. Automation, structured data capture and integrated workflows don't just reduce cycle times – they break the one-to-one relationship between loan count and operational cost. That's where the operating leverage comes from.

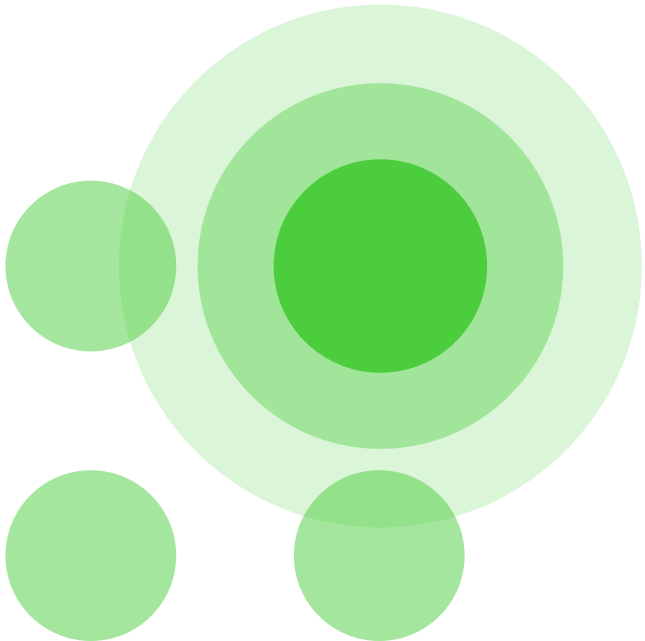
The boarding discipline: A loan's cheapest moment is its first

Here's a principle that doesn't get enough attention: a loan boarded cleanly is cheap to carry and safe to monitor for its entire life. A loan boarded poorly is expensive and opaque from day one, and it compounds every quarter.

The boarding moment – when deal terms, covenant structures, rate mechanics and fee schedules are captured into the servicing system – is the single highest-leverage point in the post-close lifecycle. Get it right, and downstream accruals, rate resets, payment notices and covenant tests run cleanly. Get it wrong, and you're chasing manual corrections across every subsequent lifecycle event.

The discipline required isn't complicated, but it is deliberate. Loan terms need to be captured as structured data, not as text in a document repository. Covenants need to be codified as testable conditions, not summarised in a PDF. Fee schedules need to be mapped to the system's calculation engine, not transcribed into a spreadsheet.

Firms that treat boarding as an operational event rather than a data architecture decision pay for it every month they carry the loan. At a portfolio of hundreds of facilities, the cumulative cost is significant, and it shows up in the wrong places: exceptions, adjustments, rework and audit-trail reconstruction burdens.



Covenant monitoring as risk management, not administration

Covenant monitoring is where operational weakness becomes credit risk.

According to McKinsey's Global Private Markets Report, covenant-lite transactions rose to 21% of direct lending deals in 2025, up from 4% in 2023. That shift means the covenants that remain carry more weight per deal, not less. Missing a breach, or catching it late, is no longer an administrative inconvenience – it's a risk management failure.

Yet across much of the market, covenant monitoring still lives in spreadsheets. Tests are run manually, often quarterly, often by analysts who are also managing boarding, amendments and investor reporting. At low portfolio volume, this is manageable. At scale, it's a liability.

Automated, continuous covenant testing changes the risk profile of a portfolio. When breach conditions are structured at boarding and tested systematically against live data, monitoring becomes a control rather than a task. Early signals surface before they become credit events. The covenant package becomes a genuine risk management tool rather than a compliance checkbox.

For institutional LPs conducting operational due diligence – and according to Ocorian's 2026 analysis, more than 60% now include dedicated operational due diligence workstreams alongside credit review – the question isn't whether you monitor covenants. It's whether you can demonstrate that the monitoring is systematic, auditable and independent of manual intervention.



The servicing maturity curve

Private credit servicing operations don't sit at a single point of maturity. They move through recognizable stages, and understanding where your operation sits is the first step to knowing where the leverage is.

Stage 1: Fragmented. Servicing runs across disconnected systems, spreadsheets and manual processes. Lifecycle events are tracked in email threads and shared drives. Reconciliation is constant. Audit trails are reconstructed, not maintained.

Stage 2: Connected. Core systems are in place, but integration is partial. Data flows between servicing and accounting require manual intervention at key points. Reporting is periodic rather than real-time. Boarding is more consistent but still not fully structured.

Stage 3: Automated. Servicing workflows run with high levels of straight-through processing. Lifecycle events trigger downstream accounting entries without manual steps. Covenant testing is systematic. Exceptions are managed by exception, not by default.

Stage 4: Intelligent. The operating model is fully integrated across servicing, accounting, data and investor reporting. AI-assisted monitoring surfaces anomalies before they require human escalation. The cost-to-serve per loan falls as AUM grows. Investor reporting is a product of the servicing infrastructure, not a separate manual exercise.

The move from Stage 1 to Stage 2 typically reduces rework and exception volume. The move from Stage 2 to Stage 3 is where operating leverage begins. The move from Stage 3 to Stage 4 is where the cost-to-serve curve bends away from AUM growth entirely.

Most firms in private credit today sit at Stage 2, with elements of Stage 1 still present in specific asset classes or vehicle types. The competitive advantage belongs to those reaching Stage 3 and beyond.

Servicing as the engine of investor transparency

Every figure an LP sees – NAV, portfolio exposure, performance attribution, audit trail – is ultimately a servicing output. The quality of investor reporting is a direct function of the quality of servicing data.

That connection is now a fundraising reality. Ocorian's 2026 analysis of institutional LP behaviour found that nearly 80% of institutional LPs expect more frequent, granular and data-rich reporting than they did five years ago, covering exposure-level transparency, collateral monitoring and independent valuation support. The same research found that over 70% of institutional investors rank transparency, reporting quality and valuation governance among their top criteria when selecting or re-upping with managers.

Reporting quality is now treated as a proxy for operational quality. LPs aren't just reading the numbers – they're reading what the numbers say about the infrastructure behind them.

For private credit managers, this creates a specific obligation: servicing can't be a back-office function that feeds a front-office reporting team. It has to be the single source of truth from which investor-facing outputs flow automatically, consistently and with a complete audit trail. When a valuation is challenged or an audit is triggered, the ability to trace it back through the servicing record – without reconstruction – is the difference between a credible answer and a compliance gap.



Five actions for senior leaders

The argument above points to five specific decisions that senior leaders in private credit should be making now.

Measure your fully loaded cost to serve per loan. If you don't know this number, you can't manage it. Track whether it falls as AUM grows – if it doesn't, you have a scaling tax.

Treat boarding as a data architecture discipline. Capture loan terms, covenants and fee structures as structured data at closing. The quality of everything downstream depends on what's captured at boarding.

Move covenant monitoring out of spreadsheets. Systematic, automated testing against structured covenant terms isn't a technology luxury – it's a risk management requirement at scale.

Locate your operation honestly on the maturity curve. Knowing where you sit is the precondition for knowing what to fix. Commit to the next stage with a specific plan, not a general aspiration.

Design servicing across the full lifecycle with a single source of truth. Codified terms, native interoperability between servicing and accounting, and a connected reporting infrastructure aren't separate projects. They're the same project.

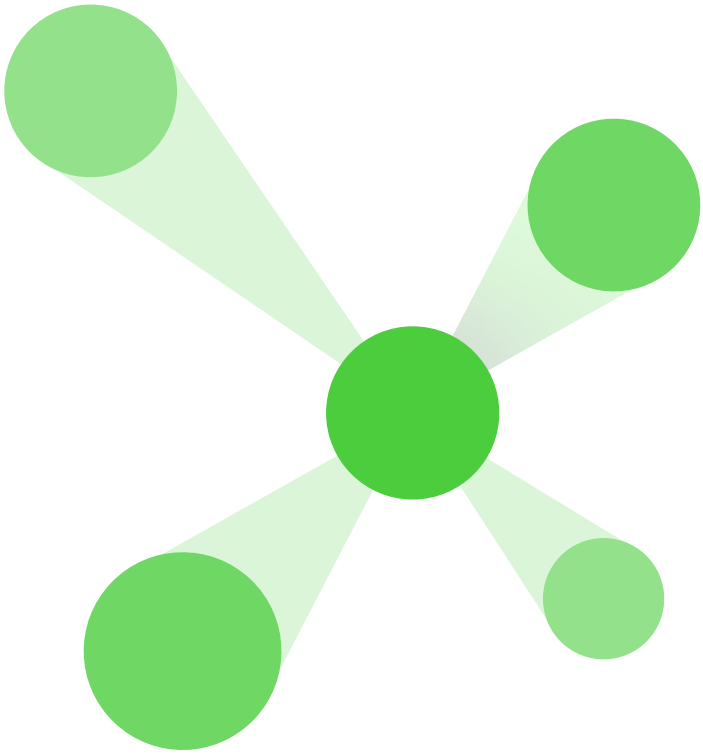


The competitive window is open – but not indefinitely

The firms building servicing infrastructure now are building a durable advantage. As the market scales, as LPs raise their operational bar, and as spread compression removes the yield cushion that once absorbed inefficiency, the cost of under-investing in servicing will become visible – in margins, in investor conversations and in the ability to compete for institutional capital.

FIS® Commercial Loan Servicing for Private Credit is purpose-built for this moment. As the servicing core of the FIS Private Credit Ecosystem, it connects loan servicing with accounting, data and investor reporting across the full loan lifecycle, supporting complex structures, frequent amendments and institutional-grade auditability without replatforming as portfolios grow.

If you're ready to understand where your servicing operation sits on the maturity curve – and what it would take to move it forward – speak with our private credit team.



Learn more

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Unlock seamless integration and human-centric digital experiences while ensuring efficiency, stability, and compliance as your business grows.

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