CovenantLab Analytics

The Hidden Alpha in Every Private Credit Contract

Future of Alpha · 2026

- Elham Saeidinezhad (Colin Powell School | CCNY)
- Uri Ravid (Columbia University)

The Blind Spot

Every risk in private credit is priced — except the one you spent weeks negotiating.

$2T+

Private credit outstanding

Every dollar lent against a negotiated covenant package.

4–8

Weeks per deal on covenant documentation

Leverage tests. CF sweeps. RP blockers. Incremental debt caps. All negotiated. All enforceable. All unpriced.

$?

Of that value in your pricing model

Duration risk: priced.
Credit quality: priced.
Covenant structure: negotiated, held — never priced as return.

The alpha the Future of Alpha conference is looking for is already in the contract — disguised as protection. Every covenant you negotiated is return waiting to be priced. Until now.

How We Think About Covenant Structures

CovenantLab Framework

The Core Logic

A covenant is a trigger.

It fires when the borrower crosses a threshold — leverage, cash flow, or behavior.

A trigger gives the lender a right.

The right to renegotiate, accelerate, block distributions, or demand repayment.

A right is return.

Blocking equity leakage before distress changes your expected recovery. That change in recovery is worth basis points. Those basis points are alpha — not insurance.

The Covenant Discount Adjustment (CDA)

CDA is the bridge between protection and return. It converts the entire covenant package into a single basis-point number — the extra return already negotiated by the lender, never credited by the market. Two framings, same number: the fair discount rate exceeds the contractual spread by CDA bps. Equivalently, the lender earns CDA bps of alpha the yield doesn't show.

The Five Protection Layers

Layer	What It Controls	How Protection Becomes Return
MT	Leverage & coverage ratios	Quarterly tripwire fires before distress deepens — lender gets renegotiation rights early
CFP	Cash flow use & sweeps	Excess cash auto-deleverages the borrower — limits equity leakage, accelerates recovery
GV	Distributions & new debt	Blocks dividends and junior creditors when leverage is elevated — preserves lender's asset base
EX	Exit & call premium timing	Make-whole and call protection lock in the lender's return if the borrower exits early
EN	Priority & enforcement rights	Anti-layering and collateral provisions prevent new creditors from jumping the queue

Each layer converts structural protection into earned return. Together they define the covenant alpha already in the contract — not yet in the yield.

Application I: Asset Management · Step 1: The Deal

A Representative Mid-Market Direct Loan

Deal Profile

Precision Components Holdings

Mid-cap industrial manufacturer · $280M LTM revenue

Loan size	**$150M Senior Secured Term Loan**
Pricing	**SOFR + 575 bps (floating rate)**
Tenor	**5 years (originated Q1 2023)**
Structure	**LBO · Sponsor-backed · Direct lender**
Rating	**B+ / B (S&P / Moody's)**
Originator	**Regional direct lending fund (~$2B AUM)**

The deal prices at SOFR+575. The lender already negotiated 52 bps of return through this covenant package. Step 2 shows how that protection becomes a yield the market hasn't credited yet.

Covenant Package (from signed credit agreement)

Covenant (contractual term)	Layer	How Protection Becomes Return
Leverage maintenance ≤5.5x, quarterly tested	MT	Quarterly tripwire fires before distress deepens — lender gets renegotiation rights early
50% excess cash flow mandatory sweep	CFP	Surplus cash auto-deleverages the business — limits equity leakage and accelerates recovery
Restricted payments blocked if leverage >4.5x	GV	No dividends or sponsor payouts when leverage is elevated — preserves the lender's asset base
Incremental debt hard cap ≤1.0x EBITDA	GV	Prevents new creditors from jumping the queue — locks in lender's seniority and priority

MT = Maintenance Testing · CFP = Cash Flow Pacing · GV = Governance

Application I: Asset Management · Step 2: TDR Valuation

Protection Already Earned. Not Yet in the Yield.

+52 bps in earned return already in this contract— not yet in the yield

Maintenance covenant ≤5.5x, quarterly	**+22 bps**
50% excess cash flow mandatory sweep	**+12 bps**
RP blocker + incremental debt cap	**+18 bps**

SOFR+575 + 52 bps CDA → SOFR+627 fair value

Design partners apply CDA to their entire book — every deal, every vintage. The protection is already in the contract. CDA puts it in the return. That is the edge.

Precision Components Holdings · Covenant Return Breakdown

$150M Sr. Secured TL · SOFR+575 · 5yr · B+/B

Covenant (contractual)	Earned return
Leverage maintenance ≤5.5x, quarterly	+22 bps
50% excess cash flow mandatory sweep	+12 bps
Restricted payments blocked if >4.5x	+8 bps
Incremental debt hard cap ≤1.0x EBITDA	+10 bps
Contractual Alpha (CA)	**+52 bps**

Duration-adjusted price impact: +52 bps × 4.2yr × 0.01 = +$2.18 per $100 face

Two lenses, one number:

As extra return: you hold a loan worth SOFR+627 that pays SOFR+575. The 52 bps is covenant alpha — earned at signing, never credited in the spread.
As discount rate: the fair yield for this loan's covenant package is SOFR+627. At SOFR+575, the market under-requires by 52 bps.

Application II: Hedge Funds & Relative Value · Step 1: The Setup

Same Sector. Same Rating. Different Contract.

Both originated Q3 2021. Mid-market industrials. B+/B rated. Both direct lendings. The market sees two loans in the same sector. TDR sees two very different contracts.

	Loan A · Direct Lending · Cov-Lite	Loan B · Direct Lending · Cov-Heavy
Loan size	$300M	$300M
Pricing	SOFR + 525 bps	SOFR + 525 bps
Maint. covenant	None (cov-lite)	≤5.5x leverage, quarterly
EBITDA addbacks	Unrestricted	Capped at 15%
RP blocker	None	Yes: blocked if leverage >4.5x
Incremental debt	Incurrence-based basket (loose)	Hard cap: ≤1.0x EBITDA
Market price	$99.25 (secondary)	$97.50 (secondary)

VS

Market prices them $1.75 apart on spread. TDR shows Loan B earns an additional 38 bps in return through its covenant package — invisible in the spread. Step 2: the signal. →

Application II: Hedge Funds & Relative Value · Step 2: The TDR Signal

Two Loans. One Signal. $2.36 Mispricing.

Loan B earns 38 bps in return through its covenant package. The market doesn't see it — it prices the loan at a discount to Loan A. That discount is the opportunity. The market has priced the contract, not the protection. TDR corrects that.

Loan A · Cov-Lite · DL	
Market price	**$99.25**
Maintenance covenant	**None (cov-lite)**
EBITDA addback cap	**Unrestricted**
OAS (covenant adj.)	**−9 bps**
Duration adj. price	**−$0.38**
TDR fair value	**$98.87**
EXPENSIVE · $0.38 overpriced · SHORT	

VS

Loan B · Cov-Heavy · DL	
Market price	**$97.50**
Maintenance covenant	**≤5.5x, quarterly**
EBITDA addback cap	**Capped at 15%**
OAS (covenant adj.)	**+38 bps**
Duration adj. price	**+$1.60**
TDR fair value	**$99.10**
CHEAP · $1.60 underpriced · LONG	

Trade: Long Loan B / Short Loan A. The covenant is not insurance — it is return. The contract is the source.

Application III: Investors & Allocators · Step 1: The Comparison

Same Secondary Market. Different Contract.

Healthcare services sector. B/B+ rated. Both 2022-vintage senior secured TLs trading in secondary (Q1 2024). The sector is identical. The covenant package is not.

Term Loan A · $175M · SOFR+620	
Issuer sector	**Healthcare services**
Rating	**B+ (S&P)**
Vintage	**2022 · Senior secured**
Market price	**$97.25 (Q1 2024 secondary)**
Maint. covenant	**None**
EBITDA addbacks	**Uncapped (no limit)**
Enforcement rights	**Standard incurrence only**

VS

Term Loan B · $200M · SOFR+650	
Issuer sector	**Healthcare services**
Rating	**B (S&P)**
Vintage	**2022 · Senior secured**
Market price	**$93.50 (Q1 2024 secondary)**
Maint. covenant	**≤5.0x leverage, quarterly**
EBITDA addbacks	**Capped at 15%**
Enforcement rights	**Acceleration + cure rights**

Same sector. Same secondary market. TL A looks higher-spread — but its covenant package earns the lender nothing. TL B's lower spread masks 48 bps of earned return. Step 2: CDA makes it visible. →

Application III: Investors & Allocators · Step 2: The CDA Decision

What the Secondary Market Can't Tell You

CDA exposes a $2.94 / $100 fair value gap — in opposite directions. The higher-spread loan earns nothing from its contract. The lower-spread loan earns 48 bps in return before you count the spread.

AVOID · $175M TL · SOFR+620	
Market price (secondary)	$97.25
Maintenance covenant	**None**
EBITDA addback cap	**Uncapped**
CDA (4.2yr duration adj.)	**−22 bps / −$0.92**
CDA fair value	$96.33
EXPENSIVE · $0.92 overpriced · AVOID	

BUY · $200M TL · SOFR+650	
Market price (secondary)	$93.50
Maintenance covenant	**≤5.0x, quarterly**
EBITDA addback cap	**Capped at 15%**
CDA (4.2yr duration adj.)	**+48 bps / +$2.02**
CDA fair value	$95.52
CHEAP · $2.02 underpriced · BUY	

CDA gap: $2.94 per $100 notional. TL B's 48 bps CDA is not a protection premium — it is return already earned through the covenant package, invisible to the secondary market. Design partners who price the contract at origination capture this return before the market discovers it. The protection IS the return.

Application IV: Regulators & Standard Setters

Building the Infrastructure Private Credit Needs

01

TRACE for Private Credit

TRACE brought price transparency to bond markets in 2002. Private credit still has no equivalent. CDA — covenant value in basis points — is the pricing unit that makes exchange listing viable.

02

Mandatory CDA Disclosure

Require CDA alongside spread in deal filing, exactly as duration and DV01 are required in fixed income. Covenant-adjusted yield becomes standardized, auditable, and regulatorily examinable.

03

Enabling Retail & ETF Access

Covenant pricing satisfies the disclosure requirements that currently exclude private credit from retail fund structures. CDA is the layer that unlocks the next $1T+ in addressable capital.

04

Rules-Based Covenant Standards

Covenant packages are priced today by convention, not methodology. CDA converts negotiated terms into a reproducible, auditable adjustment — the foundation for any rules-based standard.

Key Findings

What the CovenantLab Research Establishes

01	**The Framework**	TDR (Total Discount Rate) is the first systematic, auditable framework to price covenant structure as a return component.
02	**Covenant Alpha Is Quantifiable**	It is return the lender already negotiated — measurable, auditable, and currently uncredited in the yield.
03	**Covenant Quality Determine Recovery**	The covenant package — what lenders negotiated at origination — is the dominant factor in what they recover at default. No market signal currently captures this.
04	**LMEs Confirmed the Measurement Target**	Landmark LMEs (Revlon, Serta Simmons, Envision Healthcare) revealed what cov-lite documentation delivers under adversarial conditions.
05	**Capture Alpha Before the Market**	The alpha is already in the contract. CovenantLab prices it.

CovenantLab Analytics

Who we are

An analytics project focuses exclusively on the pricing of private credit contract structure. We develop and apply the Total Discount Rate (TDR) methodology across direct lending, CLO, and secondary market contexts.

The methodology

CDA converts covenant protection into earned return — expressed as a basis-point adjustment to the deal yield. The protection you negotiated was always there. CDA makes it visible in the number.

The open question

Private credit has scaled into a $2T+ market on the premise that negotiated structure adds value. The covenant package is that structure. It has never been priced.

If it has value — and it does — should it not appear in the return?

We are here to discuss.

elham@ccny.cuny.edu
ur2144@columbia.edu