



Private Markets Meet Structured Finance

Franklin Templeton's \$1.5 Billion CFO May Be a Sign of Things to Come

Franklin Templeton (NYSE: BEN) just closed a \$1.5 billion transaction that deserves more attention than the headline suggests. The firm's first Collateralized Fund Obligation, or CFO, pools private-market exposures from Lexington Partners (its secondaries platform) and Benefit Street Partners, or BSP (its private-credit business), in a structured vehicle run by Franklin Templeton Investment Solutions.

At first glance, this looks like one more acronym-heavy structured-finance deal. It is more than that.

The CFO sits where three large forces reshaping capital markets converge:

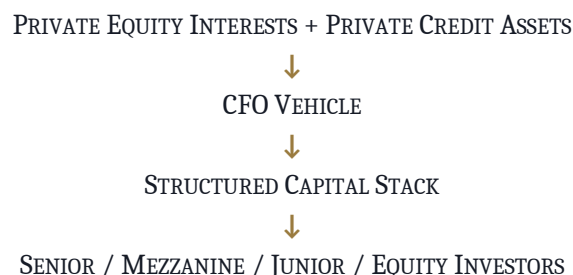
1. the growth of private assets;
2. investors' demand for liquidity and yield; and
3. Wall Street's long habit of turning illiquid assets into securities a wider universe of investors can own.

In plain terms, private markets are borrowing a page from the CLO playbook. If CFOs scale, the effects will reach well past Franklin Templeton: to private-equity managers, credit managers, insurers, wealth platforms, secondary investors and the broader capital markets.

01 What Exactly Is a CFO?

Most capital-markets participants know the collateralized loan obligation: a CLO owns a diversified pool of loans and finances them by issuing securities of varying seniority and risk. A CFO applies the same idea to private-fund interests and other private-market assets. The idea itself is not new; a handful of CFOs priced in the early 2000s. What has changed is scale: the asset base and the investor demand behind these structures are far larger today.

Conceptually:



The underlying assets throw off cash — interest, dividends, realizations, fund distributions — and that cash moves through a contractual waterfall. Senior investors get paid first. Junior investors take more risk for higher expected returns; equity sits at the bottom and keeps whatever remains after the CFO meets its obligations.

The result: a pool of assets that are individually illiquid can support securities built for investors with very different risk appetites.

02 Franklin Templeton's \$1.5 Billion Transaction

Franklin Templeton Structured Solutions 2026, L.P. raised \$1.5 billion from global investors. Two affiliates supply the exposure: Lexington Partners contributes private-equity secondaries and continuation-vehicle exposure, while BSP contributes exposure to U.S. private-credit strategies. Franklin Templeton Investment Solutions serves as collateral manager, Evercore acted as structuring adviser and placement agent, and Simpson Thacher served as issuer counsel.

The Lexington–BSP pairing is deliberate. Lexington brings the potential for seasoned private-equity exposure through secondaries and continuation vehicles. BSP brings credit assets that produce contractual current income. Put the two together and the CFO offers:

current cash yield + seasoned private-equity NAV + future realization upside

That combination may be more financeable than a vehicle built solely around newly originated fund commitments.

03 A Simplified Numerical Example

Franklin Templeton has not disclosed the transaction's capital structure, so the numbers below are illustrative only. Assume a CFO owns \$1.5 billion of private-market assets:

TABLE 1

Illustrative Collateral	Amount
Lexington secondary PE interests	\$750 million
Lexington continuation vehicles	\$300 million
BSP private credit	\$450 million
Total	\$1.500 billion

Assume the \$1.5 billion collateral pool is supported by the following hypothetical capital stack:

TABLE 2

Illustrative Capital Structure	Amount	Illustrative Cost/Return
Senior securities	\$750 million	6.0%
Mezzanine securities	\$300 million	9.0%
Junior/preferred capital	\$225 million	12.0%
Equity	\$225 million	Residual
Total	\$1.500 billion	

Again, these are not the Franklin terms; they simply show the economics. Actual CFOs may use multiple classes of debt and subordinated capital — the four-layer stack here is purely a teaching device. Suppose the portfolio earns a 10% economic return, or \$150 million a year. The illustrative annual return or carry requirement of the first three layers runs to about:

- Senior: $\$750\text{M} \times 6\% = \$45\text{M}$
- Mezzanine: $\$300\text{M} \times 9\% = \$27\text{M}$
- Junior: $\$225\text{M} \times 12\% = \$27\text{M}$

Total = \$99 million

That leaves about \$51 million (before fees, expenses and timing differences between realized and unrealized results). Against \$225 million of equity, that is a theoretical 22.7% residual return.

That is structured-finance leverage doing what structured-finance leverage does. A 10% return on the collateral does not mean a 10% return to every investor; the CFO redistributes the underlying risk and return across the capital structure.

04 Of Course, Leverage Works Both Ways

Run the same CFO through a bad year. Suppose the \$1.5 billion portfolio loses 8% of its economic value, or \$120 million. If the senior and mezzanine securities stay money-good, most of that loss falls (as designed) on the bottom of the structure. Against \$225 million of equity, \$120 million is roughly 53% of the original equity capital.

That is the other side of CFO economics.

*Structured finance does not eliminate private-market risk.
It reallocates it.*

The distinction matters. The senior tranche may trade like structured credit; the equity tranche behaves more like leveraged private-equity NAV. Same vehicle, radically different investments.

05 Why Secondaries and Credit Work Together

Private-equity secondaries suit CFO structures unusually well. Compare two portfolios. Portfolio A holds commitments to ten newly formed buyout funds: capital gets drawn over several years, distributions are uncertain, and real exits may sit five to ten years out. Portfolio B holds 100 seasoned secondary positions bought at an average fund age of six years, plus continuation vehicles holding mature companies.

Portfolio B offers several structural advantages:

- greater visibility into underlying assets;
- shorter expected duration;
- more diversified vintage exposure;
- potentially earlier distributions;
- reduced blind-pool risk; and
- more observable NAV.

Those traits matter when you are trying to finance a portfolio. Lexington's secondaries franchise is therefore more than another source of private-equity exposure. It is financeable private-equity inventory.

BSP adds the missing ingredient: cash flow. Assume \$450 million of our hypothetical CFO represents private-credit exposure ultimately backed by middle-market and senior-secured loans generating a 10% gross yield. That slice alone generates about:

$$\text{\$450M} \times 10\% = \text{\$45 million of annual gross interest income.}$$

Private-equity distributions, by contrast, arrive in lumps — one quarter heavy with realizations, the next nearly empty. Credit supplies a steadier stream of cash to service the CFO's interest while the private-equity book matures. The logic is simple:

Private credit provides the cash flow. Private equity provides the upside.

Expect that template to recur in future CFO structures.

06 Why Franklin Templeton May Be the Biggest Winner

Franklin Templeton is not merely buying assets and securitizing them. It owns a broad ecosystem of alternative-asset managers: Lexington runs secondaries, BSP runs private credit, Clarion Partners runs real estate. Franklin Templeton Investment Solutions can assemble portfolios across all of them, and the firm's global distribution arm can sell the resulting products to institutions, wealth platforms and other investors.

That creates a powerful flywheel:



This is one reason we see the deal as more than a one-off financing. Franklin Templeton has described the close as establishing a new capital-formation channel for its private markets platform. Take that language seriously.

07 The Potential “Double Monetization” of Alternative Assets

Asset managers have always earned fees by managing capital. Structured finance opens a second seam: managing the financing architecture around the assets as well. Consider our \$1.5 billion CFO. If the underlying funds earn an average management fee of 1.0% of NAV, that is:

$$\text{\$1.5B} \times 1.0\% = \text{\$15 million annually.}$$

If the CFO collateral manager earns another 25 basis points, that adds:

$$\text{\$1.5B} \times 0.25\% = \text{\$3.75 million annually.}$$

The manager can be paid at several levels of the structure. The precise economics depend on whether the CFO acquires interests in affiliated funds, separately managed exposures or other assets, and on any fee offsets or waivers. But the strategic value runs past the added fees: a successful CFO also creates fresh demand for the manager’s underlying products. That may prove the bigger prize.

08 The Critical Question: Who Buys These Securities?

The investor base is what makes CFOs intriguing. Traditional private-equity funds demand long lockups, capital calls, uncertain distributions and thin liquidity — terms that fit some institutions and repel others. Structured securities can convert slices of private-market exposure into instruments shaped to a given investor’s requirements.

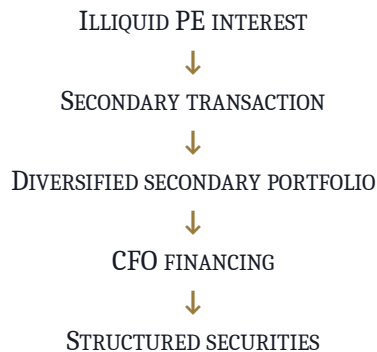
An insurer might not want raw private-equity risk, yet happily own a highly rated security backed by a diversified private-market pool, especially at an attractive spread over similarly rated corporate credit. For insurers, however, headline yield is only part of the equation. Ratings, capital charges, statutory accounting treatment and the relationship between spread and required capital may determine whether CFO senior tranches become a niche allocation or a major new source of demand. Regulators have noticed too: U.S. insurance regulators have been examining how rated structures backed by private assets should be treated for capital purposes, and that answer will shape demand as much as spread does. A family office might prefer the mezzanine. An opportunistic credit fund might buy the junior securities; a private-markets specialist might take the equity.

One collateral pool, sliced into exposures for very different buyers. That is precisely what securitization did for mortgages, loans and consumer receivables.

09 CFOs, NAV Lending and the Search for Private-Market Liquidity

Private markets have a liquidity problem. Companies stay private longer; exits have slowed; holding periods have stretched; LP distributions have disappointed; fundraising has gotten harder. Continuation vehicles and secondaries emerged as partial answers. CFOs add another.

The progression is worth tracing:



Each step pulls another pool of capital into the ecosystem. None of it magically makes the underlying assets liquid. But it may make their cash flows and risks financeable — a distinction that will matter more and more.

Set CFOs alongside the rapid expansion of NAV financing. Both markets answer the same fact:

Trillions of dollars of valuable assets sit trapped inside illiquid private-market structures.

NAV loans solve the problem through borrowing; CFOs attack it through the structured capital markets. Picture a PE portfolio worth \$1 billion. A NAV lender might advance \$200–\$300 million of debt against it. A structured-finance deal might instead carve several classes of securities out of the same economic pool. NAV lending generally places financing directly against an existing private-market portfolio; a CFO can go further by transforming portions of that portfolio's economics into securities that can be distributed across the capital markets. We expect the two markets to keep converging.

10 The Real Risk: NAV, Valuation and Correlation

Spend your diligence time here. Assume our \$1.5 billion CFO carries \$750 million of senior securities. At inception, senior debt is only 50% of collateral NAV:

$$\text{\$750M} \div \text{\$1.5B} = 50\%.$$

Now let private-market valuations fall 20%. NAV drops to:

$$\text{\$1.5B} \times 80\% = \text{\$1.2 billion}.$$

The same \$750 million senior position now represents:

$$\text{\$750M} \div \text{\$1.2B} = 62.5\% \text{ of NAV}.$$

A 30% decline takes NAV to \$1.05 billion and pushes the ratio past 71%. Nothing needs to default for the structure to become materially more leveraged. That is why valuation methodology, overcollateralization tests, distribution-diversion mechanics and manager discretion can matter every bit as much as the headline yield. The uncomfortable question is correlation: in a severe downturn, PE marks can fall at the same time credit defaults rise and exit activity slows, simultaneously reducing collateral value and the cash available to service the structure.

Valuation deserves its own scrutiny. CLOs hold loans with observable market prices. Private-equity interests are different: their values rest on portfolio-company valuations, fund marks, transaction assumptions and manager judgment. That sets up a real tension. Structured finance leans on measurable collateral tests; private equity leans on periodic valuation judgments. CFOs marry the two.

Investors therefore need answers to a hard set of questions:

- Who marks the assets?
- How frequently?
- Can third-party valuations be required?
- What happens when GP marks become stale?
- How are continuation vehicles valued?
- What happens to the waterfall if NAV falls through a trigger?

Those provisions decide whether a CFO behaves defensively in a downturn or amplifies the stress.

11 The Tax Architecture Could Be Just as Interesting

The tax-structuring questions run deep. A CFO that combines private-equity partnerships and credit assets raises issues of:

- partnership taxation and effectively connected income;
- withholding and blocker design;
- UBTI for tax-exempt investors;
- debt-versus-equity characterization and original issue discount; and
- PFIC/CFC exposure and the treatment of different classes of securities.

The same CFO can look very different to an insurer, a pension, a sovereign, a U.S. taxable investor and a non-U.S. investor — which is why tax architecture can become part of product design rather than an afterthought.

12 What Investors Should Ask

Before investing in a CFO, spend less time on the acronym and more on five plain questions.

What exactly do I own?

Look through the CFO to the underlying funds, companies, loans, vintages and managers.

Where am I in the waterfall?

A 7% senior security and a 20%-target-return equity security backed by the same assets are fundamentally different investments.

What happens when NAV falls?

Understand the coverage tests, cash traps, deleveraging requirements and distribution-diversion provisions.

Where does liquidity come from?

Credit interest? PE distributions? Asset sales? Refinancing? The answer matters. Remember, too, that the securities themselves are typically privately placed, so secondary-market liquidity should not be assumed.

Who controls the marks?

In private markets, valuation methodology feeds directly into leverage tests and cash distributions.

13 What We Would Watch Next

Franklin Templeton's first transaction will help show whether CFOs can move from niche product to a real capital-markets category. We would watch:

Ratings. Can CFOs consistently generate investment-grade — and especially highly rated — senior securities?

Insurance demand. If insurers become repeat buyers, the addressable capital base expands sharply.

Pricing. The economics turn on the spread between underlying private-market returns and the cost of structured capital.

Collateral expansion. Do CFOs stay PE-secondary products, or push into private credit, real estate, infrastructure and other alternatives?

Repeat issuance. One \$1.5 billion transaction is interesting. A recurring issuance program is a market.

Manager adoption. If Apollo, Blackstone, KKR, Ares and the other big platforms pursue similar structures, CFO issuance could accelerate quickly.

Relative value. The ultimate test is whether investors are adequately compensated — relative to similarly rated corporate credit, CLOs and other structured products — for the added complexity, valuation uncertainty and liquidity risk.

14 Our Take

CFOs will not turn private equity into a liquid asset class, and they do not erase the risks of leverage, valuation uncertainty and illiquid collateral. That misses the larger point. Modern capital markets grow by separating an asset's economics from the form in which investors must own them. Mortgages became mortgage-backed securities; corporate loans became CLOs; consumer receivables became ABS. Private credit is already flowing into structured products. Private-fund NAV can follow the same path.

Franklin Templeton's \$1.5 billion CFO may matter less for its size than for what it represents. Private markets spent two decades becoming an enormous asset class; the next phase may be turning more of those assets into capital-markets instruments. If that happens at scale, the winners will not just be the firms with the best investment strategies. They will be the platforms that can do all three:

Originate the assets, structure the capital and control the distribution.

Franklin Templeton now has a credible claim on all three. That is why this transaction is worth watching.

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