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Private Credit volatility creates an opening for broadly syndicated loans

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The private credit market has experienced a volatile start to the year. Private credit managers entered the year optimistic that M&A activity would return and dealmaking conditions would become more constructive. Instead, they have faced a rapid increase in redemption requests at retail-focused private credit funds, continued competition from the broadly syndicated loan (BSL) market and renewed expectations of interest-rate increases, rather than a much-anticipated easing cycle.

DC Advisory's US Private Capital Markets team and LevFin Insights, part of CreditSights, recap the principal market developments, including:

- **Retail outflows are putting pressure on private credit pricing and market sentiment**
- **Higher private credit costs are driving borrowers back to the BSL market**
- **Elevated interest rates and subdued LBO activity continue to challenge private credit growth**

Retail-focused funds face record redemption requests

Redemptions at retail investor-focused funds dominated private credit headlines in the first few months of the year. These investment vehicles, mainly non-traded BDCs, generally repurchase up to 5% of outstanding shares each quarter, providing shareholders with liquidity in an otherwise illiquid asset class.

Concerns over private credit exposure to asset-light, AI-exposed business models, as well as broader credit-quality concerns, led investors to redeem record amounts of money in Q1 and Q2 2026[i]. Many BDCs enforced their 5% quarterly caps in both those periods, preventing investors from fully exiting the funds*. The resulting headlines contributed to a new narrative of lost confidence in private credit.

Even as retail jitters rattled the market, institutional LPs largely remained committed to the asset class, driven in part by the longer investment horizons of pension funds and insurance companies relative to individual investors*.

Redemptions pushed private credit pricing higher

With redemptions forcing the large lenders that operate most prominent non-traded BDCs to rethink fund positioning, hold sizes at private credit firms were scaled back[ii].

As a result, credit spreads for upper-middle-market and large-cap borrowers widened. An issuer's spread is the amount above the Secured Overnight Financing Rate, "SOFR" or "S," that is used to determine the effective interest rate. Larger private credit borrowers are now being charged S+500-525 bp, compared with relatively tight new-deal spreads of S+450 bp in late 2025*.

Private credit volatility opens the door to the BSL market

The biggest blow to private credit portfolios, however, may not be redemptions, but the renewed ability of banks to poach private credit deals[iii]. While this year's volatility temporarily paused the private credit-to-BSL pipeline, the BSL market quickly reopened.

As pricing in the private market remains more expensive for larger companies, those same issuers are increasingly turning to the BSL market, where effective interest costs would be lower.

Spreads for single-B rated companies, which are generally seen as a comp to private credit borrowers, stood at approximately 325 bp in July, according to LFI data*. When compared to recent private market pricing, issuers can save 125-150 bp or more in interest in the BSL market versus private credit.

A $4.1bn BSL deal for drug developer Catalent was one of the largest private credit-to-BSL deals*. As LFI has reported, in December 2024, the company previously tapped direct lenders for a $4.2bn term loan and a $600mn revolver to fund its acquisition by Novo Holdings*.

By contrast, very few deals have gone from the syndicated market to the private credit sphere, according to LFI, which tracks the volume of BSL loans repaid by private credit money*.

None were tracked in March, May and July. Approximately $2bn moved back to private credit in April with PLZ Corp., a Caa1/CCC-rated issuer, accounting for about half of the April tally. With those ratings, there was little chance a deal would get done in the syndicated market, effectively forcing the issuer into the private credit market*.

Of the $3.5bn of BSL money repaid in June by private loans, about $3bn came from three borrowers across deals that had been expected to close for some time, with two of them dating as far back as December*.

LBO activity in private credit remains slower than expected

Away from attractive refinancing conditions, the BSL market is also winning LBO transactions, which remain subdued in the private credit market.

In July, FDH Aero closed a $1.1bn term loan B supporting Audax Private Equity's acquisition of the company, LFI reported*. The acquisition had previously been financed in the direct lending market.

Many private credit firms have up to 30% of their portfolios in software and technology, making it one of the asset class's preferred sectors. AI-related concerns have largely frozen that industry for direct lenders*.

This has created challenges for lenders looking to monetize these positions. Fewer sponsor-backed transactions limit the natural set of buyers, while AI has scrambled the math on exiting via a sale to a strategic. The same is true of AI-exposed, asset-light companies, even if they are not squarely in the software or technology sector*.

Interest rates are expected to remain elevated

CreditSights expects no cuts for the rest of the year, possibly into the first half of 2027.

At the start of the year, CreditSights anticipated a 75 bp reduction on concerns of a weakening labor market*. Now, inflationary pressures related to the US-Iran war and tariffs, along with a better-than-expected labor market in the first half of the year have meaningfully shifted the picture. Even as the market prices in some near-term rate hikes, following the loss of 23,000 jobs in July (against an expected gain of 80,000), CreditSights anticipates that the Fed will hold policy steady at the September meeting[iv].

While investors will get higher yields on their credit positions, issuers looking to raise capital in the private credit or broadly syndicated loan markets, both of which are floating rate, face more expensive borrowing costs than if the Fed were to gradually ease rates.

What to watch: US midterms, tariffs and sectors with lower AI exposure

Three developments bear watching during the second half of the year: the US midterm elections, changing sector preferences among financial sponsors and evolving US tariffs and trade policies.

We believe Democrats may hold a stronger position heading into the 2026 midterm elections, though recent redistricting may dampen the historical precedent of the president's party losing seats in midterm elections. While the CreditSights base case outcome is a gridlocked Congress, we believe the market will be looking for any signals that a regime shift in 2028 is likely.

Even as earnings have held up amid elevated tariffs, uncertainty resulting from evolving tariff policies and trade relations with key partners remains critical to the macroeconomic outlook[v].

After several years of significant dealmaking by private equity and private credit firms, transaction activity in the software sector has slowed*. Many sponsors and lenders are increasingly focusing on established sectors such as industrials and manufacturing, including businesses within the AI infrastructure value chain.

Key contacts

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What lies ahead for the European Market?

European credit markets delivered another strong quarter with Broadly Syndicated Loan market volumes totalling €62 bn in Q3 2025. This brought year-to-date volumes to €211 billion, already surpassing full-year 2024 totals, the previous high.

DC Advisory's European Debt Market Monitor: 'Turning the Tide', provides an optimistic outlook for debt markets across Europe for 2026, citing stable financing conditions, improved market sentiment, and a strong M&A pipeline.

Access the full report >

References

***All deal references and quantitative data has been sourced from LevFin Insights, a CreditSights company**

Unless otherwise indicated, all data referenced in this article is from LevFin Insights and Covenant Review. Covenant Review is a sister publication of LevFin Insights and tracks the strength of protective covenants in private credit agreements. All deal references and quantitative data have been sourced from the LevFin Insights database.

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