High Five – 2025 Outlook (Second of a Series)

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What we learned about 2024 is that many worries identified by analysts and market observers came to naught. Rates, economic growth, and inflation – all areas of concern last January – are in good shape as 2025 rolls out. More robust job growth than expected (see our *Chart of the Week*) is just one example. As one banker observed recently, what were headwinds have become tailwinds.

The focus now is on mostly global rather than domestic issues. Tariffs, trade, and geopolitical risks are taking center stage. Some of these are theoretical but could mirror events from 2017-2020. And while the rise of bond yields since the election suggest higher inflation to come, capital markets remain full speed ahead. Or as a recent Apollo research report put it, “firing on all cylinders.”

We also confirmed (and others learned) that public and private markets can each perform well without one side stealing from the other. Banks focus on larger syndicated corporate deals, and direct lenders on buy-and-hold traditional and upper middle market LBO financings. That distinction was highlighted by the broadly syndicated market’s record $1.6 trillion of loan volume last year, per LSEG LPC, of which only $84 billion – about 5% – represents new PE buyouts.

Data from our friends at PitchBook LCD support this thesis. They report 2024 new-issue leveraged loan volume (ex-repricings) of $500 billion, a level not seen since the market top three years ago. Buyout and corporate M&A financings totaled $133 billion, or 26% of all activity – the lowest in over a decade, the exception being 2023’s $70 billion.

This means we should reorient our thinking about supply and demand in the loan market. Capital formation is now more associated with process and predictability. Sponsors seek speed and certainty of execution. They align financing partners with specific borrower needs for growth and acquisition capacity, expanding lender groups as required over time to meet those needs.

We’ve said before that capital tends to fill a vacuum. Demand in the world of private credit is not a capped resource. Deployment gets triggered by the supply of new deals, and vice-versa. With continuing appetite for the asset class, growing M&A flow will be met with direct lenders offering constructive terms.

Finally, while we expect M&A deal flow to continue to improve, as global 3Q 2024 numbers highlighted, Lincoln International raised a cautionary note. “Surveyed groups [reported] that anecdotal close rates for 2024 deal launches were the lowest many could recall, with the most optimistic estimate being that only 50% of deals launched in 2024 have closed or are on track to close and the most pessimistic estimate at a paltry 30%.”

Clearly the preparation and intention for deals to launch haven’t translated to actual launches, no doubt due to gaps in valuation expectations between buyers and sellers.

Next week we turn to the first of our five themes characterizing the 2025 outlook: *Still higher for longer*: What slower rate cuts mean for private capital investors.