

# CREDIT CONDITIONS



Q4 2024

## INTRO

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Welcome to this edition of *Credit Conditions*, a quarterly publication from [McDermott Will & Emery](#) that analyzes recent debt market trends.

## IN DEPTH

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### KEY DEBT MARKET TRENDS

#### Interest Rates: Certainly Uncertain

The Federal Reserve closed 2024 with two additional quarter point rate cuts, [ending the year as expected with a top line rate of 4.50%](#). The new year began on less secure footing with [rate cuts on pause](#) and official Federal Reserve projections [reducing rate cuts for 2025 from 1.00% for the year](#) (the view as of September 2024) [to 0.50%](#). Concerns include [shifting expectations around the strength of the economy](#); the [stickiness of inflation](#); and the impacts of [US trade](#), budget, and immigration policies. This uncertainty has led to diverging market predictions ranging from [five quarter point cuts starting in May 2025](#) to no rate cuts and the [end of the rate-cutting cycle](#) to the Federal Reserve [increasing rates in 2025](#). It remains to be seen though which way the macroeconomic winds will blow.

#### Private Equity M&A: A New Year, a New Hope

The end of 2024 saw an active rebound for private equity M&A [with loosening credit markets](#) and declining interest rates closing some of the valuation gap between buyers and sellers. [Private equity exits ended the year up nearly 50% by count and 16% by value year over year, ending 2024 at 1,501 and \\$413.2 billion, respectively](#). Sponsor-to-sponsor deals also came back in 2024, [with sponsor-to-sponsor exits in Q3 exceeding the pre-pandemic average for the first time since interest rates began to rise in 2022](#). Bolt-on acquisition activity also remained strong in 2024, [with many private equity funds focusing on increasing value with operational efficiency improvements, particularly in the middle market](#). US investors also drove an increase in European private equity in 2024, [with deal values up 24% year over year](#).

Even with the rebound, many 2021 deals are still creating headwinds for the industry. [The median portfolio company hold period in 2024 grew to four years, an eight-year high, with the median hold period for exited companies now at 5.8 years](#). One industry adviser estimates that private equity funds in 2024 sold half the investments they would have in a typical year.

The slow speed of sales has raised some concerns that sponsors may have difficulty winding down older fund vintages and may continue to turn to continuation funds to buy extra time so they can sell later in a more opportunistic market.

Overall, 2025 looks to be a promising year for the M&A market. US governmental policies on [taxes](#) and [antitrust](#) are [expected to provide tailwinds for the industry](#), though uncertainty around trade policy and tariffs may prove to be a headwind as well. Limited partner pressure on sponsors to make distributions is also expected to result in continued growth in private equity exits, with predictions for more initial public offerings and leveraged buyouts (LBOs), particularly in the second half of 2025. [Healthcare M&A is also expected to see a rebound in 2025](#), with dental, veterinary, and dermatology deals already hot in 2024 and expectations of renewed interest this year in home-based care, infusion, med spa, outpatient mental healthcare, medical devices, and pharmaceuticals.

### The BSL Market Sets Records in 2024

The broadly syndicated loan (BSL) market ended the year on a high note, with [a record-setting \\$191 billion of deals closing in December 2024](#), multiples larger than historical monthly and December averages of \$46 billion and \$27 billion, respectively. Overall, BSL market activity in Q4 2024 was the second-highest quarter on record at \$398 billion, just shy of the \$405 billion in Q2 2024. Repricings dominated the BSL market, with roughly \$800 billion – or 60% of the entire BSL market – being repriced in 2024, exceeding the prior 2017 record of \$432 billion and including 122 companies repricing more than once. Amend-and-extend transactions also set records in 2024, with [\\$226 billion for the year](#), easily beating 2023's record \$176 billion. Between amend-and-extends and refinancings, [the near-term maturity wall was reduced significantly](#), with 75% of 2026 maturities and 46% of 2027 maturities addressed in 2024. Dividend recaps similarly set records in 2024, with \$81.2 billion (a close second to 2021's \$82.2 billion) and a median dividend of \$300 million. Although 2024 dividend recaps were the highest in at least six years, that record came with a lower-than-average increase in leverage – only 1.1x in 2024 compared to an average of 1.4x the prior 10 years and peaks of 1.7x in 2011, 2014, and 2022. These trends are expected to continue in 2025 until M&A activity ramps up later in the year.

### Private Credit vs. BSL: Competitive but Complementary

The tides shifted in 2024, with the BSL market refinancing nearly \$10 billion more of the private credit market than private credit refinancings of the BSL market. Overall, the BSL market refinanced \$41.8 billion of private credit deals (a large jump from 2023's \$6.5 billion) compared to \$31.9 billion of BSL deals refinanced by the private credit market (increasing from 2023's \$26.9 billion). The broader trend of the BSL market financing larger deals continued in 2024, with the median BSL deal at a record high of \$860 million (double the median in 2014) and only 18% of loans (based on count) below \$500 million (compared to 44% in 2019). Similarly, the median closing pro forma adjusted EBITDA of borrowers in the BSL market over the past three years grew to \$300 million (compared to a median of \$163 million in 2019). On the other hand, private credit continued to dominate the market for LBO financing, with 84% of 2024's LBOs tracked by LCD funding with private credit, increasing from 65% in 2021.

Many borrowers were lured back to the BSL market by lower pricing and higher leverage, with pro forma leverage increasing to 5.2x in 2024 from a 13-year low in 2023 of 4.9x (albeit significantly less than the 6.0x peak in 2019 and the 10-year average of 5.7x). The BSL market also competed by offering terms more commonly found in private credit, such as portability and lower ticking fees and longer availability periods on delayed draw term loans (DDTLs). Traditional selling points of the BSL market, such as covenant-lite and 101 soft call for six months (compared to two years of hard call for private credit), retained their appeal as well.

The private credit market responded in 2024 by [tightening spreads](#) and [offering paid-in-kind \(PIK\) interest on day one for regular deals](#), a feature unavailable in the BSL market. The private credit market also loosened financial covenants, [with reports of some lenders offering cov-lite as low as \\$50 million EBITDA or cov-wide as low as \\$35 million EBITDA](#). Additionally, private credit retained its traditional benefits of certainty of terms (since private credit does not have pricing and other flex like the BSL market), larger DDTLs with longer availability periods, and more frequent opportunities for portability than the BSL market.

## Private Credit: Gaining Weight

Scale was the name of the game for private credit in 2024 as private credit funds, asset managers, and banks joined forces in an attempt to grow both market share and addressable markets. The largest funds were able to achieve scale, in part, by dominating funding, with the top 20 private credit managers responsible for 70% of total capital raised (compared to 36% in 2019). “If you can’t build it, then buy it” (or partner with it) was also a theme, with asset managers purchasing private credit funds (such as [Blackrock’s acquisition of HPS Investment Partners for \\$12 billion](#)) and various banks partnering with private credit managers including (1) [Citigroup partnering with Apollo](#); (2) [Wells Fargo partnering with Centerbridge Partners](#); (3) [Webster Bank partnering with Marathon Asset Management](#); and (4) [Piper Sandler partnering with BC Credit Partners](#). In many of these joint ventures, banks have taken on the role of placement agents, particularly for non-sponsored loans, similar to syndication in the BSL market but faster and for unrated loans, while giving private credit funds new opportunities to deploy their capital.

Private credit is also expanding its scope by targeting new asset classes for loans, including auto loans, aircraft leasing, consumer loans, student loans, infrastructure financing, and other asset-based financing. The industry has also shown signs of expansion on the investor side, [with some private credit funds working with banks to allow institutional investors to trade and syndicate private credit loans](#) and [CUSIP launching services for private credit debt](#). Private credit has also begun targeting investment opportunities for retail investors, [with private credit exchange-traded funds \(ETFs\) launching in 2024](#) and the [discussion of potential regulatory changes to allow private credit investments to be held in 401\(k\)s and similar retirement funds](#).

## Hybrid Financing Trends

The hybrid capital market has seen significant growth in recent years as companies seek flexible financing amid evolving economic conditions, emerging as a distinct asset class. These innovative structures, which bridge the gap between debt and equity, enable businesses to swiftly raise capital while addressing challenges such as limited debt capacity, concerns over dilution for existing equity holders, and bridging valuation gaps. Structured financing can also be advantageous in the context of acquisitions, including those facilitated through hybrid joint ventures, and in the context of financing private capital funds at the fund level. Hybrid instruments, which integrate features of both debt and equity, include preferred equity of various flavors, warrants, holdco PIK notes, and mezzanine debt. Beyond the economic terms, such as dividend rights, liquidation preferences, prepayment premiums, interest rates, and cash versus PIK interest, covenants, governance rights, and protective provisions are critical deal terms that must be customized by the parties for each unique situation. These tailored solutions have broad applicability across various industries, notably in healthcare and life sciences, technology, entertainment assets, consumer brands, and infrastructure. The use of flexible financing has certainly evolved beyond distressed situations to become a vital tool for growth, as private equity and private credit funds collaborate with issuers to develop bespoke solutions that help issuers maintain agility and optimize their growth trajectories.

## Distress and LMEs

Inflation and high interest rates took their toll in 2024, with bankruptcies at a 14-year high. Distress in the BSL market appears (at least on paper) to be declining, with payment default rates by amount and by issuer at the end of 2024 at 0.91% and 1.45%, respectively (compared to recent peaks of 1.75% by amount in July 2023 and 2.07% by count in February 2024). Payment defaults only tell a portion of the story though, as out-of-court restructurings – including liability management exercises (LMEs), which involve coercive elements like uptiering or asset drop downs – have become more common and aren't included in typical default rate statistics. For example, including LMEs in payment default rates would increase the default rate to 4.70% for 2024. Moreover, according to S&P, more than half of the defaults in 2024 were distressed loan exchanges (*i.e.*, the loan terms are changed and maturities extended to avoid bankruptcy but investors are paid back less), of which 56% were identified by Fitch Ratings as LMEs, up from 33% in 2023. Official payment defaults may also be masked in the private credit market by the increasing usage of PIK interest to address liquidity concerns before defaults develop, raising concerns that while the Federal Reserve pauses on interest rates, PIK interest could create unsustainable debt loads and defaults in the future.

## Serta Redux

The US Court of Appeals for the Fifth Circuit closed out the year with a landmark reversal of the Serta LME uptiering case. In the US District & Bankruptcy Court for the Southern District of Texas' prior decision, Judge Jones concluded that the uptiering transaction constituted an "open market purchase" under Serta's credit agreement and thus the transaction was permitted. Reversing the lower court, the Fifth Circuit reasoned that an "open market purchase" was more than just free enterprise and that the word "market" means a specific market (*i.e.*, the BSL secondary market, which was not the market where the Serta transaction occurred), and thus the uptiering transaction was not permitted.

Even in light of the Serta decision, other avenues for uptiering may still remain viable. For example, on the same day as the Serta decision, the New York Supreme Court's First Appellate Division unanimously held that the uptiering transaction in the Mitel case was permitted since, unlike the Serta case, the credit agreement did not rely upon an "open market purchase" exception but rather the credit agreement language allowed the borrower to "purchase" loans "at any time." The language in the Mitel case is more common in the bond market than it is in the loan market but is similar to language seen in some recent credit agreements where "privately negotiated exchanges" are expressly permitted and thus allow non-pro rata uptiering transactions. Other recent credit agreements have similarly permitted uptiering as long as the transaction is offered to all affected lenders. However, these approaches are less common in the market than the "open market purchase" standard found in the Serta case, and thus the Serta ruling will likely limit the feasibility of uptiering LMEs.

## KEY DEBT MARKET DATA

- [Private Credit Pricing & Leverage Data \(February 5, 2025\)](#)
- [BSL Leverage Trends Q4 \(January 7, 2025\)](#)
- [BSL vs PC Spread & Covenant Trends Q4 \(January 29, 2025\)](#)
- [BSL Documentation Trends Q4 \(January 14, 2025\)](#)
- [BSL Documentation Trends Jan 2025 \(February 3, 2025\)](#)
- [BSL A&E Documentation Trends 2024 \(February 4, 2025\)](#)

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