

Private credit's coming-of-age moment: stress, repricing, and maturity

- ▶ Private credit is entering its first true cycle after a decade of benign conditions, and the result is a market undergoing recalibration rather than crisis.
- ▶ AI-driven disruption has triggered a targeted repricing of software-exposed credit, semi-liquid funds are grappling with redemption queues and valuation lags at a time when market expectations for higher-for-longer long-term rates are tightening financial conditions and geopolitical risks are dominating headlines.
- ▶ Yet lending activity remains resilient, defaults are contained, and the income profile of private credit continues to provide a meaningful buffer. Banks are re-entering direct lending, insurers hold growing exposures, and regulators are paying closer attention, but systemic risk is low probability.
- ▶ The outlook for 2026–27 is one of adjustment: modestly higher defaults, wider dispersion across managers, continued repricing in software-heavy portfolios, and positive returns supported by income. In our view, private credit is not breaking; it is maturing into a more transparent, cycle-tested asset class.

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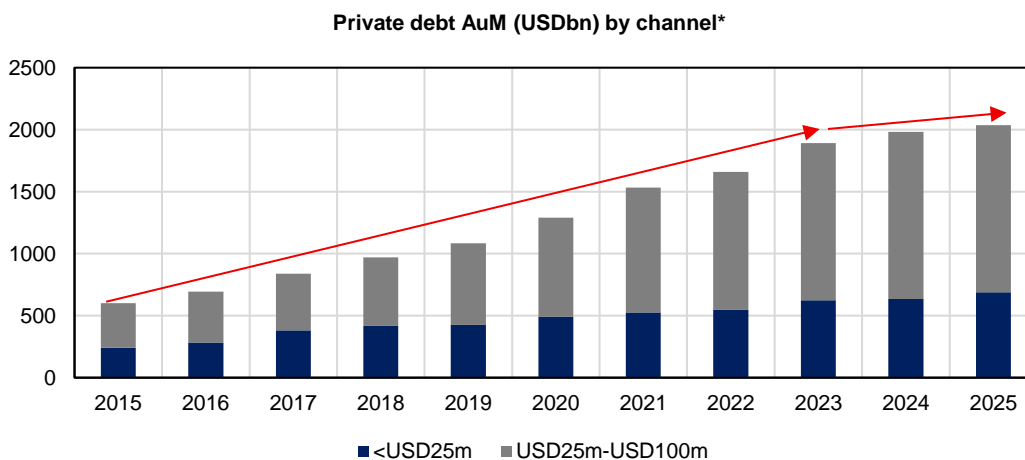
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Introduction: A maturing asset class meets its first real test

Private credit – now approaching USD3trn in assets as per MSCI – has moved from a niche alternative to a core institutional allocation. For details and discussion see our note [Private Credit: from a hidden gem to a heavyweight, May 2025](#). Its ascent was built on a decade of low interest rates, bank retrenchment, and a global search for yield that followed the Global financial crisis of 2008-2009. That benign backdrop has now given way to the most complex test the asset class has faced. AI-driven disruption is challenging the resilience of software borrowers. Semi-liquid private credit funds are confronting redemption queues. Valuation opacity is drawing scrutiny. Long-term bond yields are expected to stay higher for longer. And banks are re-entering the direct-lending arena with renewed appetite as regulatory regime there is softening. These forces have created a market suspended between technical stress and fundamental resilience. Semi-liquid private credit funds are facing redemption pressures and publicly traded private credit firms have underperformed broader financials. Yet, the Institute of International Finance (IIF) notes that lending volumes remain steady, defaults are contained, and the income cushion embedded in private credit loans continues to provide meaningful support. The outlook is neither crisis nor complacency. It is a recalibration.

Exhibit 1: Private debt AuM rose sharply till 2023 and expanded further subsequently, albeit at a slower pace



Source: Pitchbook | Notes: *Including capital from private wealth and insurance investors, global private debt AuM is now approaching USD3trn.

The software shock: targeted, not systemic

The most visible stress episode emerged in early February, when Anthropic’s release of open-source plug-ins triggered a sharp repricing of software-exposed credit. Listed Business Development Companies (BDCs) with higher software exposure underperformed peers in a clear, linear pattern. According to MSCI, a hypothetical BDC fully concentrated in software would have underperformed one with no exposure by roughly 13ppt in Q1’26. Adjusting for leverage reduces the implied decline in underlying software credit to about 6%, suggesting the market was not rejecting private credit as an asset class but rationally repricing a specific borrower segment.

This matters because software represents a substantial share of private credit portfolios – often 25% to 30%. These companies tend to be more leveraged, more dependent on growth expectations, and more vulnerable to technological disruption. According to Oxford Economics, an overall 25%-35% of the overall private credit portfolios are subject to AI disruption risk. The IIF highlights that AI-related pressures could push private credit defaults higher given this concentration. Yet many loans to software firms sit at the top of the capital structure, providing meaningful valuation cushions even after repricing. And not all software companies are equally exposed. Firms with proprietary data, entrenched customer relationships, or mission-critical functions remain more resilient. Software is the epicentre of current stress, but the shock is targeted, fundamentally explainable, and partially cushioned by seniority and income.

Exhibit 2: Software services segment has underperformed not only its other tech peers but also the broader equity market as AI-disruption fears took hold

Equity index performance over the past two years



Source: MSCI, LSEG Workspace, and ADCB Asset Management

Semi-liquid funds: Liquidity mismatch moves to centre stage

The most acute pressure point in private credit today, arguably, is not credit performance but liquidity structure. Semi-liquid private credit funds – evergreen BDCs and similar vehicles – have grown according to IIF to roughly USD0.4trn, expanding access to insurers, wealth channels, and retail investors. These structures offer periodic liquidity despite holding inherently illiquid assets, creating a structural tension that has now surfaced. Record redemption requests, gating mechanisms, and withdrawal caps have become more common, while NAV-timing mismatches have amplified investor anxiety. Accordingly, several major BDCs – including Blue Owl, Ares, Apollo, Blackstone, and KKR – have already capped withdrawals.

The dynamic resembles a slow-motion run. Investors may be redeeming not because fundamentals have deteriorated, but because they fear being last in the queue. NAVs are reported with a quarter-lag, meaning investors often make decisions based on stale valuations. While this does not constitute

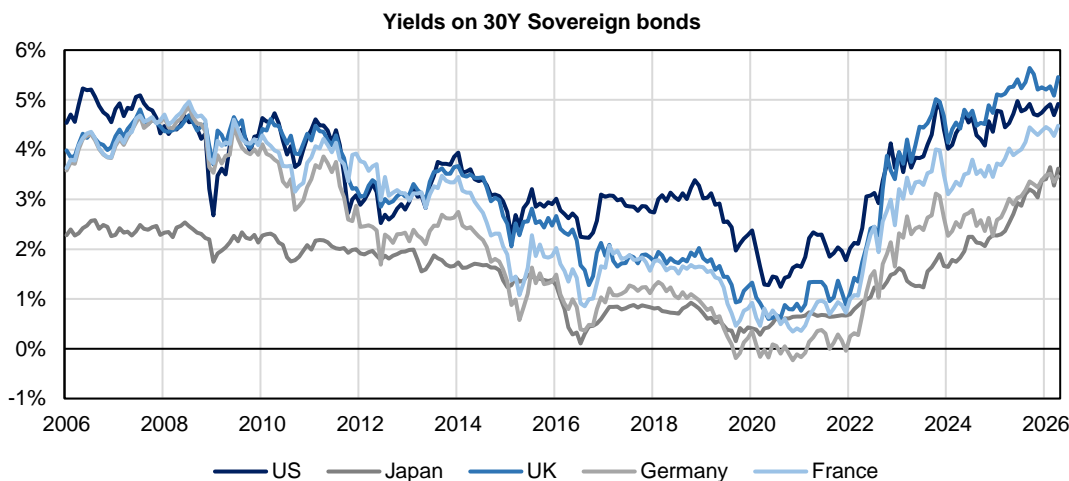
systemic risk in the 2008 sense – given low leverage and limited interconnectedness – it is a structural vulnerability that will shape the next phase of the industry’s evolution, in our view.

Defaults, valuations, and the higher-for-longer regime

Default rates in private credit remain contained for now. IIF data shows that private credit defaults have broadly tracked high-yield defaults, with recent declines driven more by selective defaults – such as payment-in-kind arrangements – than outright failures. Nonetheless, higher long-term interest rates and AI-related disruption could push defaults higher, particularly in software-heavy portfolios.

Valuations are also under pressure. Publicly traded private credit firms have underperformed financials and high yield markets, reflecting investor scepticism about valuation methodologies and the opacity inherent in private markets. The higher-for-longer long-term bond yields environment, which was absent for a long time following the global financial crisis, compounds these pressures. Also on the short-term interest rates, expectations of Fed rate cuts and rising energy-driven inflation have tightened financial conditions. Higher rates reduce the relative attractiveness of illiquid credit, increase refinancing risk for borrowers, and compress valuation multiples. Yet the income profile of private credit remains compelling. MSCI estimates that IT-sector private credit loans yield roughly 9.6%, providing a meaningful cushion even under moderate write-down scenarios.

Exhibit 3: Long-term bond yields have moved meaningfully higher in the present cycle vs. the previous cycle



Source: LSEG Workspace, and ADCB Asset Management

Bank re-entry and the competitive landscape

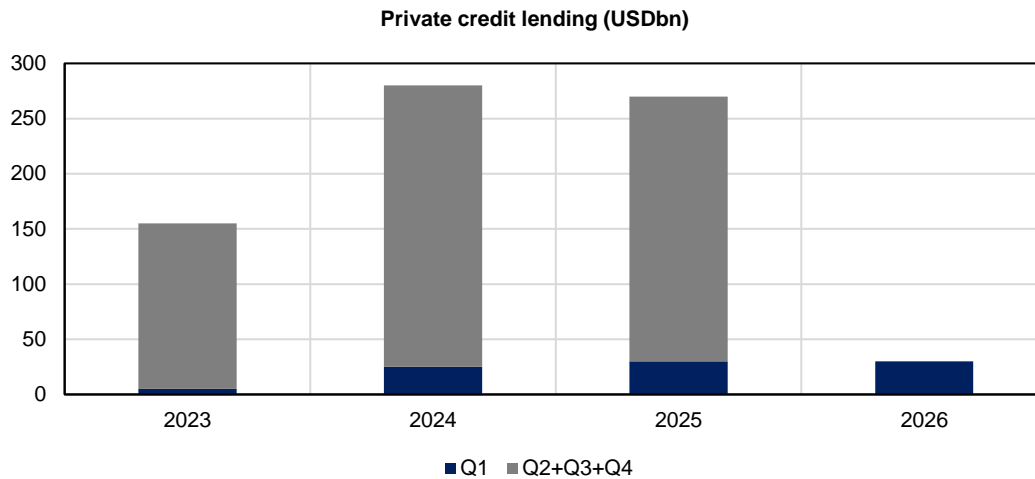
The easing of US leveraged lending rules in late 2025 is drawing banks back into direct lending. This shift is likely to intensify competition for deal origination, compress spreads, and push private credit firms toward deeper partnership models with banks. The competitive landscape is evolving. Private credit is no longer the sole source of capital for middle-market borrowers, and the market is evolving into a more integrated ecosystem where traditional and alternative lenders increasingly operate side by side.

Systemic risk: at worst, a slow burn, not a flashpoint

The debate over systemic risk in private credit is increasingly polarized. Reuters highlights concerns that insurers – who hold around 35% of US insurer assets in private credit – could face a slow erosion of solvency if defaults rise. The contagion channel, even at its worst, would not resemble bank-run dynamics but rather a gradual deterioration in retirement security. Systemic risk remains limited: leverage is modest, exposures are dispersed, and assets and liabilities are better matched than during the 2008 crisis. The truth likely lies between these poles. Private credit is unlikely to trigger a sudden systemic event, but

valuation opacity, liquidity mismatch, and insurer exposure create slow-moving vulnerabilities that will likely attract increasing regulatory scrutiny. Worth noting that despite all the headlines, private credit lending this year has been at par with the previous years' run rate.

Exhibit 4: Private credit lending in 2026 has been at par with 2024-25



Source: IIF and ADCB Asset Management

Outlook: A repricing phase, not a collapse

Taking all these together, we think that private credit is entering a new regime defined by greater dispersion, heightened transparency demands, and more realistic pricing of risk. Several constructive forces remain in place. Income generation is strong. Structural protections and seniority continue to matter. Borrowers' performance remains solid across many sectors. Institutional demand is growing. Bank partnerships are expanding the ecosystem. New pricing tools are improving transparency. At the same time, headwinds are significant. AI-driven disruption in software, higher-for-longer long-term rates, semi-liquid fund redemption dynamics, NAV-pricing mismatch, rising regulatory scrutiny, and renewed bank competition all weigh on the outlook. In our assessment, the base case for 2026-27 is one of adjustment and not of dislocation or distress. Defaults are likely to rise, but not in a wave. Dispersion between managers will likely widen. Software-heavy portfolios will continue to reprice. Returns are likely to be stable to modestly positive, supported by income. The industry will continue evolving toward better transparency and more robust liquidity management. For private credit asset class that is coming of age, this is a stress test, not a systemic unravelling.

Conclusion: the asset class grows up

Private credit is transitioning from a decade of benign conditions into its first real cycle. The sector's vulnerabilities – sector-specific exposures, liquidity mismatch, and valuation lag – are now visible. But so are its strengths: income resilience, structural protections, and a diversified investor base. The next phase will reward managers with disciplined underwriting, portfolios with balanced sector exposure, funds with robust liquidity design, and investors with a medium-term horizon.

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