Q1 2026 Leveraged Loan Market Overview

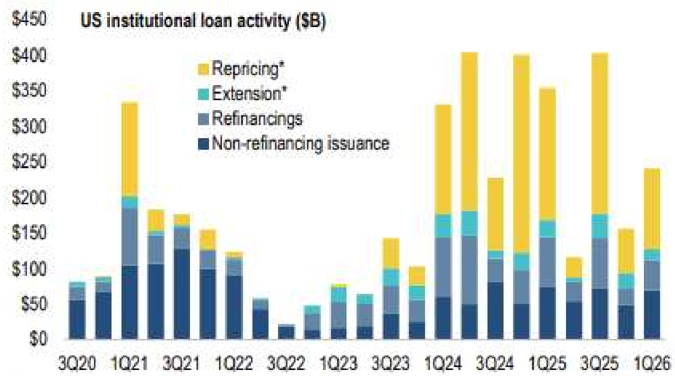
Under Pressure: Leveraged Loans Navigate Volatility to Start 2026

May 6, 2026

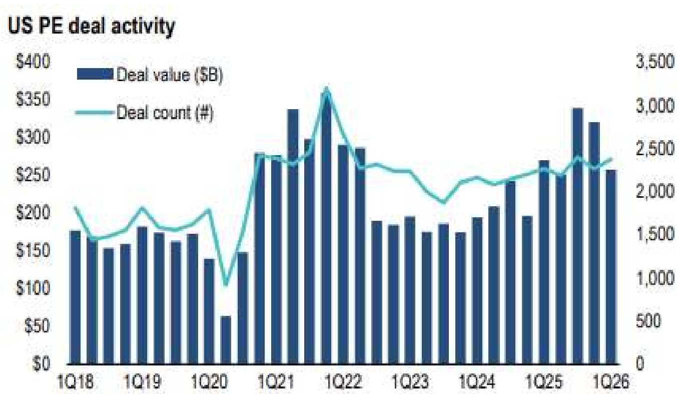
Q1 2026

LEVERAGED LOANS NAVIGATE VOLATILE START TO 2026

The leveraged loan market entered 2026 with activity moderating from last year's elevated levels, as heightened volatility and a broader risk-off backdrop weighed on refinancing ("refi") and repricing volumes. The anticipated M&A resurgence has developed more slowly than expected due to tariff and trade policy uncertainty, AI-disruption concerns, geopolitical tensions (including the Iran war and its impact on oil prices), and diminished expectations of near-term Fed rate cuts. Measurable loan demand in Q1'26 fell to its lowest level since Q3'24 driven by negative retail fund flows, though CLO issuance held up. Additionally, credit quality divergence between lower and higher rated borrowers continues to grow. Lower-rated borrowers face the most maturity pressure yet have made the least progress addressing maturities as spreads widen and sentiment deteriorates. In Q1'26 the US syndicated loan asset class shrank to $1.53 trillion, contracting ~1.3% from Q4'25 for the largest quarterly decline in just over three years.



Source: PitchBook | LCD • Data through March 31, 2026
*Reflects repricings and extensions done via an amendment process only



Source: PitchBook • Geography: US • Data through March 31, 2026 • Uses extrapolated deal sizes

Source: PitchBook | LCD • Data through March 31, 2026

LEVERAGED LOAN ACTIVITY WITHSTANDS VOLATILITY

Institutional loan activity in Q1'26 totaled $241 billion, an improvement from a slow Q4'25, though trailing Q1'25 by 32%. Most notably, repricings were limited in Q1'26 due to heightened volatility and a risk-off sentiment, with additional pressure from software sector headwinds. Nonetheless, refis and non-refi issuance both rose q/q, while net new issuance came in at $69.7 billion, only 5% behind last year and ahead of 2024 and 2025 quarterly averages. This suggests that deal-driven activity has held up well in the first quarter, contrary to what the headline figures suggest.

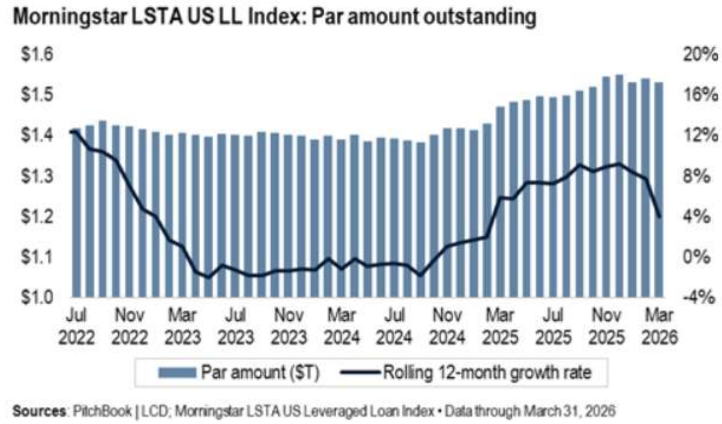
US private equity dealmaking stagnated in Q1'26 after a recovery that built through 2024 and 2025. Although deal count ticked slightly upwards over the course of the first quarter, Q1'26 represented the slowest quarter (by deal value) for PE activity since Q2'25, finishing at $257 billion across 2,375 deals (including acquisitions, add-ons, and equity growth transactions). This trailed Q4'25 deal value by more than $60 billion and translated to a slow start to the year for leveraged loan issuance.

M&A ISSUANCE SHOWS PROMISE

M&A demand remained robust as Q1'26, with the strongest opening quarter for M&A-related BSL issuance since the Fed began hiking rates in 2022. Buyout, sponsored add-on, and corporate M&A financing totaled $51.2 billion over the quarter, up slightly from Q1'25 and almost doubling Q4'25 issuance. PE sponsors alone raised $29 billion to finance buyouts – the highest reading since Q1'22 – though the slowdown in PE activity through Q1'26 has not yet worked its way through to loan issuance. Although M&A-driven issuance is showing signs of strength, $22.6 billion – more than 40% of first quarter volume – stemmed from five mega-transactions: Hologic, EA, Sealed Air, Janus Henderson, and Azuria Water.

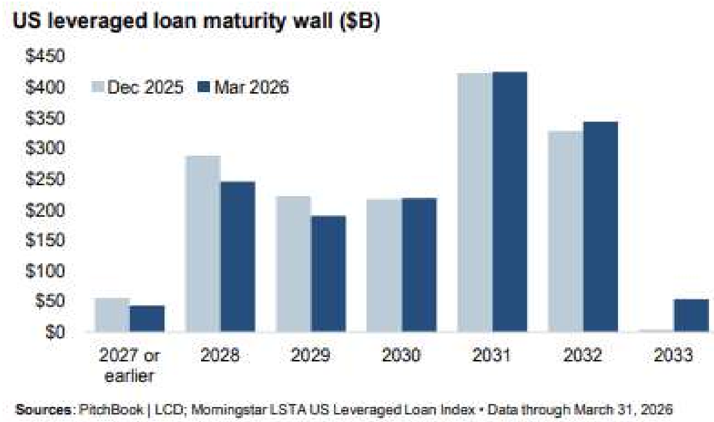
REPAYMENTS OUTPACE ISSUANCE

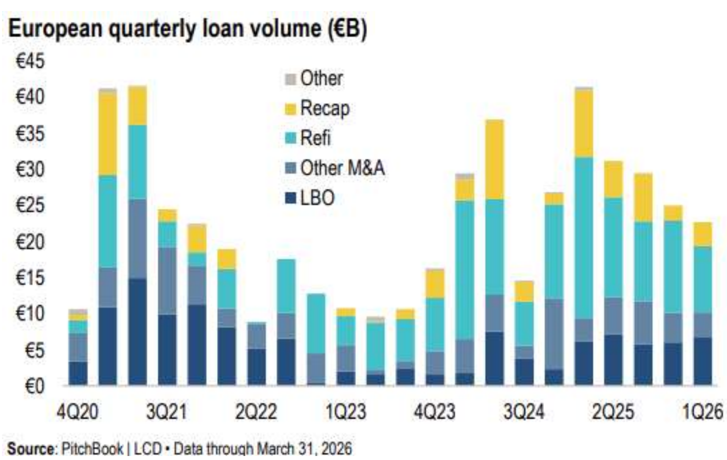
After expanding by $131 billion in 2025, net leveraged loan supply fell by $19.1 billion in Q1'26, the largest quarterly decline since Q4'22 as repayments outpaced new issuance. Net loan supply is measured as change in outstandings, per the Morningstar LSTA US Leveraged Loan Index (newly issued loans minus repayments). Par amount outstanding at the close of Q1'26 was $1.53 trillion, below the end-of-2025 level of $1.55 trillion. While multiple "megadeals" launched in March, most had not closed, remaining outside the index at month-end.



MATURITY MANAGEMENT SLOWS

In Q1'26, the 2027 maturity wall fell by 23% to $43.4 billion, while the 2028 maturity wall was cut by 15% to $246 billion, both of which were weaker than a year ago when borrowers reduced near-term maturities within two and three years by 26% and 17%, respectively. This slowdown arose as declining technical conditions and widening spreads weighed heavily on refi activity in the first quarter. New loan issuance to refi existing debt was 41% below Q1'25 and 27% below the 2024-25 quarterly average of $56.6 billion. Additionally, maturity extensions fell to $15.6 billion in Q1'26, the lowest for any first quarter since 2022.



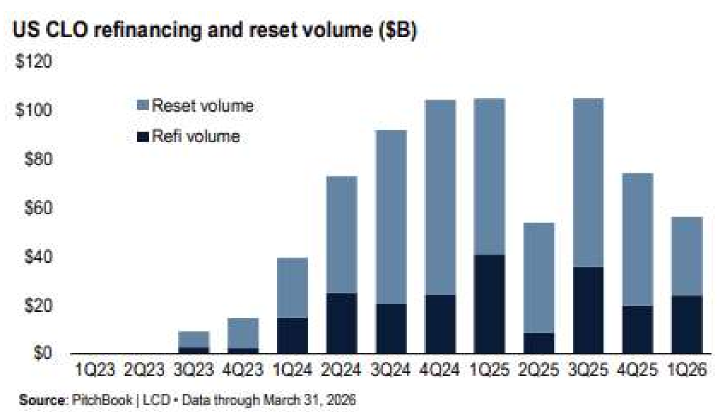


ISSUANCE: EUROPE

European leveraged loan issuance slid to its lowest Q1 total since 2023 but remained overall strong as AI-disruption, the Iran war, oil price shocks, and stagflation concerns weighed on the market. Q1'26 launched €22.7 billion of loans, a ~45% decline from the €41.4 billion in Q1'25, which was a record-breaking quarter. 82% of Q1'26 European issuance volume came before February 28, when airstrikes on Iran began, highlighting the war's significant impact on loan volume. Meanwhile, M&A-related volume totaled €10.2 billion in the first quarter, in line with the past 4 quarters while loan refinancing volume totaled €9.2 billion, contracting heavily from the €22.3 billion in Q1'25.

CLO RESETS AND REFIS TUMBLE

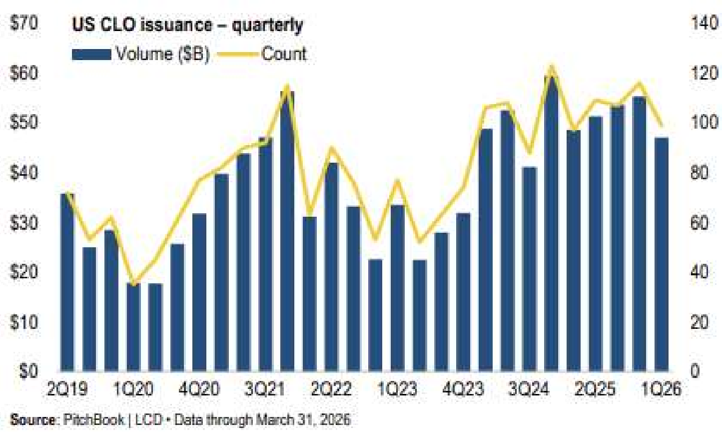
In the first quarter, CLO resets and refis were $32.2 billion and $24.0 billion, respectively, totaling $56.2 billion of activity – down more than 45% from the Q1'25 total of $104.7 billion and more than 23% from the Q4'25 total of $73.7 billion. The decline was most pronounced in March 2026 as managers priced just $6.7 billion across 14 resets over the month after pricing $25.6 billion across 54 transactions in January and February. Uncertainty in the market and higher spreads amidst the drawdown in software names made repricings less attractive in Q1'26. The trend is expected to continue as the expectations of rate cuts deteriorate.



CLO ISSUANCE LAGS 2025 PACE

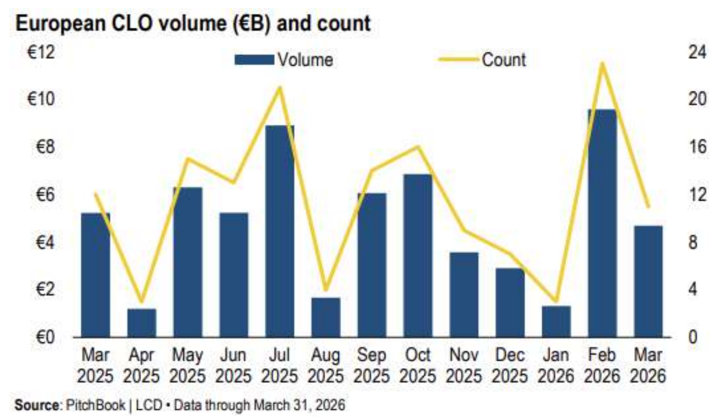
CLO issuance remained robust but pulled back in Q1'26 after three straight quarters of growth. New CLO issuance of $47.0 billion across BSL and middle-market/private credit CLOs was ~3% behind Q1'25 ($48.6 billion) and ~15% behind Q4'25 ($55.3 billion) due to growing macro and geopolitical uncertainty. Beyond issuance, CLO collateral pool quality showed early signs of stress in Q1'26: average CCC exposure rose to 5.01% from 4.81% in February; the share of obligors with negative outlooks climbed to 13.09% (highest in over a year); and weighted average loan prices in CLO portfolios fell to 95.11 from 96.89 a year prior.

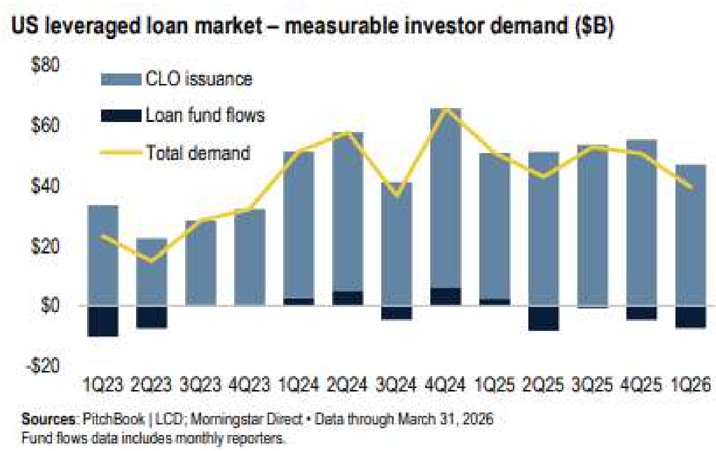
While February produced the highest monthly new-issue tally on record, European CLO new-issue volume ended Q1'26 at €15.6 billion across 37 deals, short of the €17.3 billion across 38 deals in Q1'25. The onset of the Iran war and a broader risk-off sentiment pressured the European CLO market in the latter portion of the quarter, highlighted by the steep drop in both volume and count from February 2026 to March 2026, while January marked a slow start.



LOAN DEMAND COOLS

Q1'26 was the weakest fiscal quarter in terms of total measurable demand since Q3'24, totaling $39.6 billion of demand as uncertainty and volatility surrounding Iran, rate cuts, and inflation persisted. Weakness was driven almost entirely by sharply negative fund flows, rather than floundering CLO activity. Loan fund outflows reached $7.5 billion in the quarter, while CLO issuance fell slightly to $47.0 billion after holding above $50.0 billion for most of 2025. Though below previous quarters, CLO issuance is still well above levels seen in 2022 and early 2023.



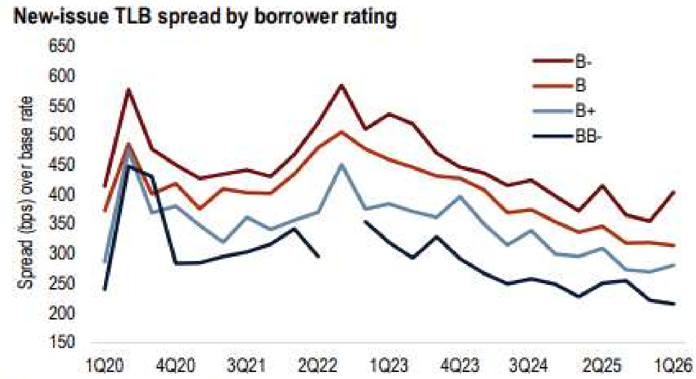


SECONDARY PRICES CRASH

Q1'26 was defined by deteriorating investor sentiment deepened by the software selloff (detailed below). After peaking in July 2025, the weighted average bid of the US Leveraged Loan Index ("LLI") entered a pronounced downturn through the remainder of the year and into 2026. By March 3rd, the index had fallen to 94.17, lower than the 94.41 seen after last April's "Liberation Day" tariffs. Prices recovered only slightly to 94.80 by March 20 before declining once again at quarter's end. Loan prices fell by 201 bps in Q1'26 alone after ending Q4'25 at an average weighted bid of 96.64. However, as of this update, secondary prices have shown signs of improvement, recovering 68 bps to 95.31 in April.

SPREADS DIVERGE

In Q1'26 overall, new-issue TLB spreads remained relatively stable, though riskier B-minus names saw spreads widen by 49 bps from Q4'25 levels to S+423 amid volatility and risk-off sentiment. However, Q1'26 figures are skewed toward January deals that pre-dated both the SaaS selloff and the onset of the Iran conflict. Looking at February and March, BB-minus and B-plus spreads widened by 38 bps and 74 bps, respectively, to S+240 and S+332. The resulting gap between these cohorts nearly doubled from 50 bps in January to 92 bps by quarter end, signaling that investors are recalibrating risk premiums.

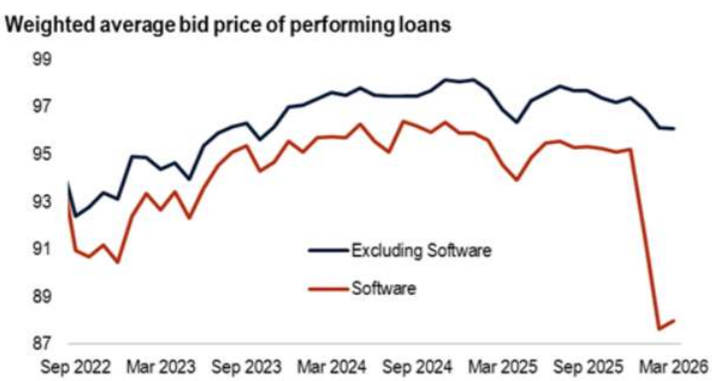


Source: PitchBook | LCD • Data through March 31, 2026

SOFTWARE DRAGS DOWN THE BROADER INDEX

The software sector, which accounts for 13% of the outstanding loans tracked by the leveraged loan index, weighed heavily on the weighted average bid following major AI-driven concerns about software and software-as-a-service ("SaaS") credits. Excluding software loans, which separately saw average bid price nosedive to 87.97, the index declined by only ~100 bps since the end of 2025 (versus 201 bps total, as mentioned in the previous section), to 96.08.

Similarly, returns of the overall US leveraged loan market turned negative to start 2026, posting a 0.55% loss in the first quarter led by steep declines in the software sector in January and February and geopolitical concerns. This represents the weakest first quarter reading since Q1'20's COVID-driven decline. Cumulative losses in software loans through February were about 7%. Though software was the fourth-best performing industry in March, posting a 1.26% return for the month, the sector's YTD loss remains at 5.85%. Making matters more difficult, software borrowers skew towards the lower end of the credit spectrum, with 47% holding a B-minus rating – more than double the percentage of B-minus loans in the broader index.



Sources: PitchBook | LCD; Morningstar LSTA US Leveraged Loan Index • Data through March 31, 2026

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LEVERAGED LOANS RETURN A LOSS

The Leveraged Loan index lost 0.55% in Q1'26, slightly lagging all other fixed-income categories. This is the weakest first-quarter return for leveraged loans since the COVID-driven collapse of Q1'20. However, loans declined far less than US equities, as the S&P 500 pulled back by more than 4.0% over the quarter as geopolitical tensions, AI-driven software sector selloff, and falling rate cut expectations weighed on investor confidence. Overall, the first quarter saw all asset classes produce negative returns, though LTM returns remain positive across the board.

Returns by asset class

	Mar 2026	Feb 2026	1Q'26	LTM
Morningstar LSTA US LL Index	0.54%	-0.78%	-0.55%	4.81%
Morningstar US High-Yield Bond	-1.19%	0.18%	-0.54%	7.00%
Morningstar US Corporate Bond	-2.05%	1.30%	-0.41%	4.67%
S&P 10-year Treasury Index	-2.49%	2.77%	-0.19%	3.71%
S&P 500	-4.98%	-0.76%	-4.33%	17.80%

Sources: PitchBook | LCD; Morningstar; S&P Dow Jones Indices • Data through March 31, 2026

CHALLENGES FOR PRIVATE CREDIT

Private credit faced a turbulent Q1'26 as AI-driven disruption concerns surrounding software borrowers forced lenders to confront elevated sector exposure across business development company ("BDC") portfolios. Though Q1'26 was filled with negative headlines, estimated direct lending volume increased q/q even as deal count continued its downward slide. Private credit firms now face higher spreads as lenders demand greater compensation for risk, as well as more obstacles standing in the way of attracting retail investors into the "semi-liquid" investment funds.

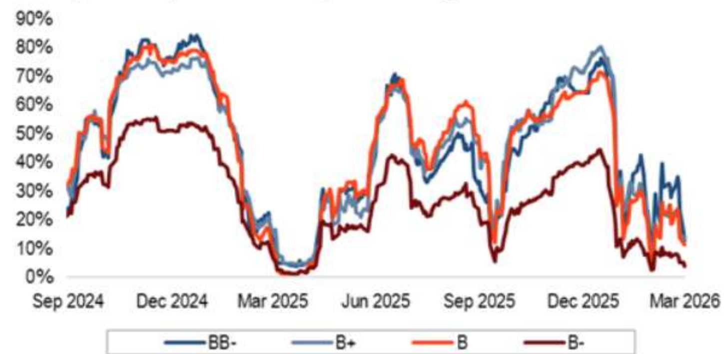
Direct lending deal count and estimated volume ($B)

Source: PitchBook | LCD • Geography: US • Data through March 31, 2026

LOANS PRICED AT PAR/ABOVE COLLAPSE

After 2025 ended with 58% of loans priced at par or above – often a proxy for strength of investor demand – the measurement cratered in Q1'26. After the first quarter, only 14% of loans were priced at par or above. Though extremely weak, the share of loans priced at par or above did bounce back from the March 2nd low of 9%. The par-or-better cohort is heavily skewed towards higher-quality borrowers, with 60% carrying a rating of B-plus or higher and none being classified as a software-sector loan. Only 13% and 4% of BB-minus and B-minus issuers remained atop par at the end of the quarter.

Loans priced at par and above by issuer rating

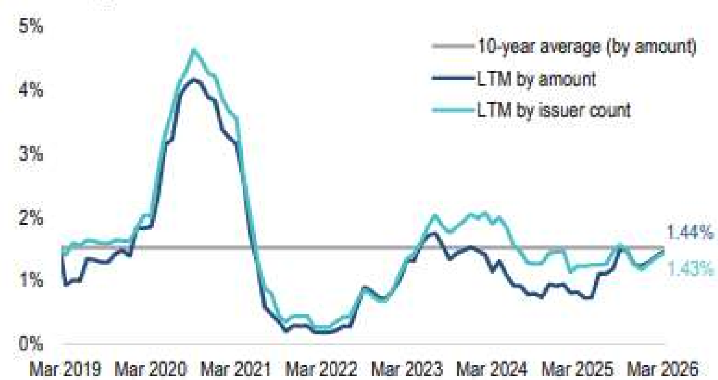


Sources: PitchBook | LCD; Morningstar LSTA US Leveraged Loan Index • Data through March 31, 2026

DEFAULT COUNT TRENDS UPWARD

The U.S. leveraged loan default rate (by dollar amount) rose from 1.23% in Q4'25 to 1.44% in Q1'26. Compared to the end of Q1'25, the payment default rate by amount increased by over 75% y/y from 0.82% to 1.44%. Additionally, the payment default rate by issuer count also rose to 1.43%, up from 1.18% in Q4'25 and 1.23% in Q1'25. Though elevated in relation to recent measurements, both the default rate by amount and issuer count remain below the index's 10-year historical averages (1.52% and 1.71%, respectively). This, however, can be partly attributed to the rise in distressed liability management exercises ("LMEs") according to LCD.

US leveraged loan default rate

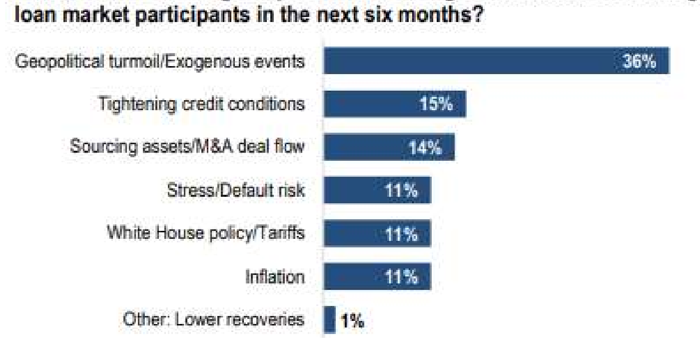


Sources: PitchBook | LCD; Morningstar LSTA US Leveraged Loan Index • Data through March 31, 2026

LOOKING FORWARD

According to LCD's Q1'26 survey, geopolitical turmoil/exogenous events is overwhelmingly the number one concern among leveraged loan market participants over the next six months (36% of votes). Tightening credit conditions, which was not a top answer in the Q4'25 survey, came in at second in Q1'26 (15% of votes), while sourcing assets/M&A deal flow remained in third (14% of votes) as borrowers continue to delay transactions.

Which of the following will present the strongest headwinds to leverage loan market participants in the next six months?



Source: PitchBook | LCD • Data through March 30, 2026

Notably, stress and default risk, which placed first in the Q4'25 survey, fell three spots to the fourth highest concern in the Q1'26 survey. Participants also continued to note White House policy and tariffs, as well as inflation, as potential headwinds, though these were considered less of a risk than other concerns.

Volatility in the leveraged loan market is likely to persist into the year as risks remain elevated across trade policy, geopolitics, and AI-driven credit concerns, particularly in the software sector. Despite LBO and M&A-driven BSL issuance reaching a four-year high in Q1'26 (based on M&A deals announced in 2025), new deal announcements and the forward M&A pipeline remain muted relative to initial 2026 expectations. Measurable demand fell to its lowest level since Q3'24. With B-flat spreads widening over the course of the quarter, borrower access to the leveraged loan market has become more costly and selective. Fed rate cut expectations have faded as inflation concerns have resurfaced amid oil price volatility stemming from the Iran war, axing a potential tailwind that was being priced into the market. Notwithstanding the turbulent macro backdrop, leveraged loan fundamentals remain sound with the observed trends viewed as right-sized market reaction. ARC continues to see robust deal activity and demand for credit insurance and economics shifting slightly in the favor of lenders.

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