STAR MOUNTAIN CAPITAL



Market Intelligence & Insights:

U.S. Bank Market Lending & Regulations Update

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Investing in the Growth Engine of America®

Regulatory Shift in Leveraged Lending: Key Market Implications

Key Takeaways

- Eased bank regulations are expected to increase competition and pressure spreads in large and upper middle-market private credit. [1]
- The lower middle-market ("LMM") remains structurally differentiated due to lower leverage, stronger covenants, and limited bank participation. [2]
- Competitive pressures from bank re-entry are expected to be concentrated in larger market segments rather than the LMM. [2]

Executive Summary

U.S. regulators have withdrawn the 2013 interagency leveraged lending guidance, which had discouraged banks from underwriting higher leverage sponsor-backed loans above roughly 6x debt to EBITDA.[1] This regulatory shift allows banks to apply their general commercial credit standards rather than a separate leveraged lending framework, increasing their flexibility to participate in more highly leveraged transactions.

Figure 1: Market Types & Their Impact

Market Type	Impact
Large / Upper Middle-Market & Broadly Syndicated Loan ("BSL") Segment	Increased bank participation, higher competition, and potential spread tightening.
Lower Middle-Market Segment	Limited bank competition due to labor-intensity and capital constraints, preserving lower leverage levels and covenants.

Given the structural inefficiencies and limited competition within the LMM segment as shown in Figure 1, the impact of this guidance and subsequent rollback is expected to be less pronounced. As a result, the LMM continues to stand out as a strong complementary allocation within a diversified portfolio.

What Changed in U.S. Bank Regulations

In 2013, interagency guidance put in place by the Office of the Comptroller of the Currency ("OCC"), Federal Deposit Insurance Corporation ("FDIC"), and the Board of Governors of the Federal Reserve System set new standards for how banks handle leveraged lending. This framework discouraged banks from pursuing the more highly leveraged sponsor-backed transactions and required stronger risk management, underwriting discipline, and ongoing monitoring for these loans. [3] The 2013 guidance was accompanied by a 2014 publication of Frequently Asked Questions ("FAQs") which provided further guidance.[4]

On December 5th, 2025, the OCC and FDIC issued a statement formally rescinding the 2013 leveraged lending guidance and the related 2014 FAQs, directing banks to manage leveraged lending exposures under general principles for safer commercial lending.[5] The FDIC asserted that these regulations were overly broad and restrictive, inadvertently capturing types of loans that the guidance was never intended to cover.

Important to note, the Government Accountability Office determined the 2013 guidance was not a formally adopted regulation. It reflected supervisory expectations but did not go through the congressional and procedural steps required to become a binding rule for purposes of the Congressional Review Act.[5]

Impact on the Large and Upper Middle-Market Deal Landscape

The rescission of leveraged lending guidance is expected to have meaningful implications for larger private credit transactions with increased competition from banks.[1] Figure 2 shows how large market dynamics can have negative impacts in large markets while having rather optimistic implications for the U.S. lower middle-market.

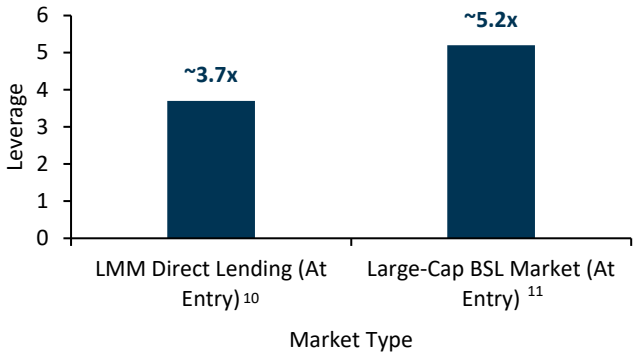
Figure 2: Large Market Effects

		Potential Impact	
Deal Effects	Description	Large Market	U.S. LMM
Bank & BSL Parity	Private credit may need to match bank and BSL pricing and terms in large deals.[6,7]	▼ Negative	▲ Positive
Spread Compression	More lender competition can push spreads down.[8]	▼ Negative	— Neutral
More Borrower-Friendly Terms	Borrowers can negotiate looser covenants and weaker lender protections to win mandates.[9]	▼ Negative	▲ Positive

Why the LMM Remains Differentiated

This leveraged lending guidance primarily constrained larger, more highly levered loans, leaving the lower middle-market unaffected because leverage tends to be lower at entry, as shown in Figure 3. The more efficient large and upper middle-market have large credits that are liquid and standardized enough in nature to fit bank balance sheets. By contrast, LMM transactions are typically smaller, with fewer lenders per deal and more intensive underwriting, which structurally limits direct bank and BSL competition.[2]

Figure 3: Entry Leverage by Market Segment



Source: CIBC, Pitchbook. September 2024. Please see endnotes for additional information.

Large banks in the United States (with $250+ bn in total consolidated assets or $10+ bn in on- balance sheet foreign exposure) are required to hold high-quality liquid assets sufficient to cover projected net cash outflows over a 30-day stress period under the Liquidity Coverage Ratio ("LCR").[12, 13] Large banks subject to the LCR have maintained levels of high-quality liquid assets above required minimums, while community and smaller banking institutions are generally not subject to the LCR.[13,14] Maintaining these liquidity buffers is balance sheet intensive, which structurally incentivizes large banks to allocate the remainder of their balance sheet toward larger, more liquid, standardized credits, rather than scaling into the LMM, thus limiting competition.

As a result, the LMM continues to maintain more lender-friendly structures, including stronger covenants and lower leverage even as competition increases in the larger market.[15] Preqin research on private debt documentation further notes that financial maintenance covenants and bespoke lender protections remain common in the LMM and have not eroded to the same extent seen in larger, more liquid markets.[15]

Portfolio Implications for Limited Partners

For limited partners, an important takeaway is that banks re-entering this market are most likely to increase competition in large and upper middle-market private credit where borrowers have the most financing alternatives, which may cause spreads and terms to be competed down. At the same time, the LMM remains structurally differentiated, with smaller transactions, fewer lenders per deal, and stronger covenants. This can protect the LMM from the spread compression that may be seen in the large and upper-middle markets. [15]

As a result, LMM investments may serve as a complementary allocation within investors' portfolios to existing larger private credit portfolio exposures that now face increased bank competition. We believe this segment of the market provides reliable income through strong lender protections and conservative structures, offering differentiated return drivers rooted in rigorous underwriting.

Endnotes & General Disclosures

Endnotes

1. OCC and FDIC Rescind Interagency Leveraged Lending Guidance. https://www.sullcrom.com/insights/memo/2025/December/OCC-FDIC-Rescind-Interagency-Leveraged-Lending-Guidance
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For further information, please reach out to: ThoughtLeadership@StarMountainCapital.com

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