

2025 Year in Review

Private Credit



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Private Credit: 2025 Year in Review & 2026 Outlook

Key Takeaways

- Following regulatory reform, non-bank institutional investors continue to replace deposit-funded banks as the primary source of capital for corporate lending, providing extended-maturity commitments matched to asset durations.
- Institutional capital now finances a broad spectrum of assets including residential mortgages, infrastructure debt, equipment financing and alternative assets like music royalties.
- Hybrid capital structures have emerged as critical solutions for private equity sponsors, generating returns comparable to upper-quartile private equity with superior downside protection.
- Looking to 2026, priority sectors include energy infrastructure, digital infrastructure, defense and national security, and next-generation manufacturing—all requiring patient institutional capital.
- Emerging opportunities in music royalties and sports franchises offer compelling risk-return profiles with long-duration, inflation-resistant cash flows uncorrelated to traditional markets.

Private Credit Growth

Following regulatory reform, corporate lending shifted from deposit-funded banks to institutional investors. Banks excel at short duration working capital with matched liquidity profiles. Institutional investors, insurance companies, pension funds and dedicated credit vehicles provide extended-maturity commitments with locked investment periods matched to asset durations, thereby eliminating the liability mismatches that create systemic vulnerability.

Where Private Credit Operates

Institutional capital finances: residential mortgages, credit card receivables, student loans, public transit infrastructure debt, aircraft equipment financing, auto loan securitizations, fleet leases, commercial real estate, franchise whole business securitizations, manufacturing equipment leases, and music and media royalty-backed financings. This breadth demonstrates that institutional lending provides essential capital for households, businesses and municipalities.

2026 Outlook: Hybrid Capital

Hybrid capital helped address portfolio liquidity constraints for private equity sponsors with 2021-22 vintage investments, which faced compressed exit markets. Structures include 45-50% preferred equity stakes, minority common positions, secured debt with equity warrants, preferred equity with participation rights and PIK/OID instruments.

Top-tier managers generated returns comparable to those of upper-quartile private equity, with superior downside protection. Joint venture frameworks achieved dual classification, receiving equity treatment from rating agencies for corporate balance sheets and investment-grade debt pricing for investors, while also creating excess spread. Structurally, senior common equity utilized shareholder agreement provisions and distribution waterfalls to establish priority without triggering the constraints of preferred equity.

Limited partners shifted from focusing on absolute returns to prioritizing risk-adjusted performance, favoring the downside protection of hybrid capital. As industrial modernization accelerates, hybrid structures provide scaled, patient capital matching extended development timelines.

Examples

- **Supporting Business Expansion:** A profitable semiconductor company experiencing strong market demand requires substantial capital to fund advanced manufacturing capacity but seeks to avoid the dilution associated with traditional growth equity rounds. The hybrid structure features convertible preferred instruments with built-in return floors through dividend accumulation rights, paired with participation in value appreciation above predetermined thresholds. This arrangement allows the management team to maintain strategic control and preserve meaningful ownership while offering investors downside mitigation through priority cash flow claims and upside exposure through conversion mechanisms.
- **Facilitating Investor Transitions:** An investment firm holding mature positions in resilient consumer businesses seeks partial monetization opportunities without completely exiting successful investments. The solution involves continuation vehicles where new capital partners acquire controlling interests while the original sponsor retains substantial minority stakes. Terms include baseline return guarantees with waterfall distribution structures and maintained governance participation. This framework enables the fund to return capital to limited partners while preserving exposure to future growth and aligns incentives between incoming investors and the established sponsor through shared economics.

2026 Outlook: Digital Infrastructure

Digital Infrastructure. The explosive growth in global data generation is driving unprecedented demand for data center capacity, fundamentally reshaping the digital infrastructure landscape. Two primary forces propel this expansion: enterprises migrating workloads from on-premise servers to cloud computing platforms and the emergence of artificial intelligence applications requiring enormous processing power.

While comparisons to late-1990s fiber overbuilds surface regularly, today's cycle is different. These transactions are long-term contracted offtake agreements with investment-grade hyperscalers, structural power and land constraints limiting speculative development, and fast refresh cycles that absorb capacity through step-function performance gains with each hardware generation.

Hyperscale data centers have dominated development, clustering in markets where power availability and grid connections create structural bottlenecks. Unlike fiber networks where marginal capacity additions carry minimal cost, data center construction remains capital-intensive with substantial ongoing operating expenses, making speculative builds economically unfeasible. The limiting factor is power rather than capital, with grid connection queues, transformer lead times and permitting difficulties preventing unconstrained overbuilds.

As AI workloads increasingly overtake traditional cloud computing as the primary demand driver, different facility types emerge to serve distinct purposes. Training models require massive computing power and are located near cheap electricity sources, while inference applications demand proximity to end users with minimal latency. Success requires controlling competitive moats including power access, entitled land, grid connections, permits and the operational expertise necessary to work with hyperscalers who consolidate relationships with trusted partners demonstrating strong execution track records. Investment discipline emphasizes unit economics after power and capital costs, long-tenor offtake agreements with take-or-pay provisions, balanced counterparty exposure and designs supporting future technology evolution rather than pursuing exposure at inflated prices in overheated markets.

2026 Outlook: Emerging Sectors

Music Royalties. Music royalties represent a compelling opportunity in the alternative investment landscape, providing access to long-duration assets that generate consistent cash flows uncorrelated to traditional market cycles. With intellectual property rights typically lasting 70 years beyond an artist's lifetime, these investments offer exceptional longevity with predictable, inflation-resistant revenue streams. What distinguishes music royalties from conventional private market strategies is their unique risk-return profile—delivering steady income without requiring an exit event to realize returns. High-quality music catalogs can be effectively self-liquidating through their ongoing yield, potentially generating mid-teen returns through distributions alone, offering more downside protection than traditional equity while providing greater upside potential than fixed-income instruments. As asset-backed investments, they provide ownership of underlying copyrights and

licensing agreements while outsourcing operational responsibilities to third-party administrators, creating a passive income stream with built-in inflation protection.

Sports. Sports franchises have evolved from passion assets into performance assets with institutionally credible cash flow profiles, generating revenue through media rights, sponsorships, premium seating, licensing agreements and integrated real estate development. This transformation has attracted institutional capital at unprecedented scale, with pension funds, insurance companies and global asset managers viewing sports as infrastructure-like investments offering entertainment-driven growth potential. Lenders are financing discrete ecosystem components—broadcast receivables, naming rights agreements, venue redevelopment projects and ancillary real estate holdings—rather than providing generalized team financing. Stadium facilities backed by long-term use contracts and naming agreements can support senior debt structures that behave similarly to project finance, with stable economics and exposure detached from competitive performance outcomes.

The opportunity extends beyond professional leagues into collegiate athletics, youth sports infrastructure and ancillary service providers entering their commercial era. The legalization of name, image and likeness rights has transformed college programs into fully commercial enterprises, requiring working capital facilities, stadium financing and sponsorship advances secured against receivables and ticket income. Youth and amateur sports generate substantial annual spending with fragmented capital formation, creating scalable credit opportunities in facility development, tournament infrastructure and training complexes driven by durable demand. Successful deployment requires fundamental discipline: diversified revenue bases, credible governance frameworks and transparent capital structures differentiate institutional-quality opportunities from speculative ventures within this maturing asset class.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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