

# Private Credit

## The hidden leverage behind the next credit squeeze

- Early loan failures (“cockroaches”) are likely signals of broader hidden stress in private credit, where high leverage—rather than the asset class itself—combined with opaque valuations and weak underwriting amplifies underlying vulnerabilities.
- The most likely outcome is not a systemic crisis but a gradual credit squeeze, as these risks surface slowly and constrain lending, weighing on growth over time, particularly in Europe.

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### Introduction

The global private credit market has grown rapidly, with estimates ranging from \$1.75 trillion to over \$3 trillion.<sup>1,2</sup> It has become a core source of non-bank lending for middle-market companies, especially as banks have retreated from riskier lending segments.

However, the sector remains opaque. Limited disclosure and the absence of market-based pricing make it difficult to assess the distribution and magnitude of risks, causing banks to be more cautious.

In recent months, senior market participants have revived the “cockroaches” analogy—popularized by JPMorgan CEO Jamie Dimon—to describe how isolated loan defaults in opaque credit markets may signal broader, hidden stress. The idea is that seeing one “cockroach” suggests many more are present but not yet visible, particularly in segments such as private credit where transparency is limited.<sup>3</sup>

### From boom to emerging stress

Private credit expanded rapidly after the Global Financial Crisis of 2008. In a low-rate environment, capital flooded into direct lending, often financing leveraged buyouts with increasingly borrower-friendly terms.<sup>4</sup> Competition among lenders led to higher leverage multiples, more optimistic assumptions about growth and valuations, weaker creditor protections, and structural features, such as payment-in-kind (PIK) interest.<sup>5</sup>

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That environment has now shifted. Higher interest rates, weaker growth, geopolitical volatility, and structural changes, including AI disruption threatening software companies that represent 23% of private credit portfolios, are exposing vulnerabilities and could amplify cyclical risks.<sup>6,7</sup>

Investor redemption requests have risen sharply, with numerous non-traded funds approaching or exceeding their 5% quarterly limits, creating a pipeline of unfulfilled requests.<sup>8</sup> The increased use of PIK structures suggests that some borrowers are struggling to meet cash obligations, effectively deferring payments rather than servicing debt.<sup>9</sup>

Market-based signals reinforce these concerns: publicly traded Business Development Companies (BDCs) are trading at an average 25% discount to net asset value, their widest margin since late 2020, indicating investor skepticism about valuations.<sup>10</sup> Meanwhile, refinancing risks are increasing for loans originated under more favorable conditions, as higher rates and weaker growth challenge earlier assumptions.<sup>11</sup> Lenders, in turn, are demanding higher risk premia, reflecting a broader assessment of credit risk.<sup>12</sup>

### **Leverage and underwriting vulnerabilities**

The most important vulnerability in private credit is elevated leverage combined with weakened underwriting standards during the expansion phase.

While newer loans originated under tighter conditions may prove more resilient, older vintages—from 2020 to 2022—remain highly susceptible to refinancing risk.

Highly leveraged borrowers now face higher borrowing costs, lower valuations, and reduced credit availability, increasing the likelihood of restructuring or gradual deleveraging.<sup>13</sup>

### **Liquidity, valuations, and correlation risks**

Liquidity mismatches, valuation opacity, and portfolio concentration amplify risks in private credit: redemption limits constrain lending as funds manage illiquid assets, delayed loss recognition obscures true valuations, and concentrated exposure—particularly to software and private equity-backed firms—heightens vulnerability to sector-specific shocks.

These dynamics suggest that risks may materialize slowly but broadly, particularly if refinancing conditions continue to tighten.

### **Transmission to the real economy**

As funds face rising redemption requests, valuation uncertainty, and weaker borrower performance, they are likely to reduce new lending and adopt more selective underwriting standards. This contraction in credit supply directly affects mid-sized firms, which have limited access to alternative financing.

For these firms, tighter credit conditions translate into higher borrowing costs or reduced access to funding altogether. In response, they are likely to scale back investment and, in some cases, employment.

The result is a gradual, persistent drag on economic activity, consistent with a slow credit squeeze rather than a sudden shock.

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### **Europe versus the United States**

The private credit market is heavily concentrated in the United States. U.S. assets under management total roughly \$1.3-1.4 trillion, around three to four times larger than Europe's €430 billion market.<sup>14</sup> Fundraising and fund domicile are similarly skewed.

Despite its smaller size, the adjustment is likely to be more challenging in Europe due to structural factors. The United States benefits from a unified legal and bankruptcy framework, established restructuring frameworks such as Chapter 11, and deeper capital markets that offer alternative financing sources for firms. These features facilitate faster and more orderly resolution of distressed debt.

By contrast, Europe's market is more fragmented across national insolvency regimes, judicial systems, tax structures, and creditor-rights frameworks.<sup>15</sup> Cross-border restructurings are slower, more uncertain, and more costly. Europe has weaker and more heterogeneous restructuring frameworks. Restructuring procedures vary widely across countries in terms of speed, court involvement, creditor hierarchy, and enforcement capacity.<sup>16</sup> Europe also has less developed capital markets and lower market depth, leaving middle-market firms more dependent on bank and private credit financing.<sup>17</sup>

While the U.S. system can partially absorb the adjustment through alternative funding sources, European firms face tighter constraints, increasing the likelihood of prolonged deleveraging and weaker investment.

In this context, a contraction in private credit supply would have a more pronounced impact in Europe, leading to slower adjustments, longer restructuring processes, and potentially stronger effects on investment and growth.

### **Systemic risk or contained adjustment**

There is an ongoing debate about the systemic importance of private credit.

Some policymakers emphasize risks related to opacity, leverage, and liquidity mismatches as a threat to financial stability.<sup>18</sup> Others argue that the sector does not currently pose a systemic threat and, as it has, so far, acted as a counter-cyclical backstop, expanding when leveraged loan markets tighten and helping stabilize credit supply.<sup>19</sup>

In practice, these positions reflect different interpretations of the same underlying issue: whether current "cockroaches" are isolated or indicative of broader hidden leverage across the system.

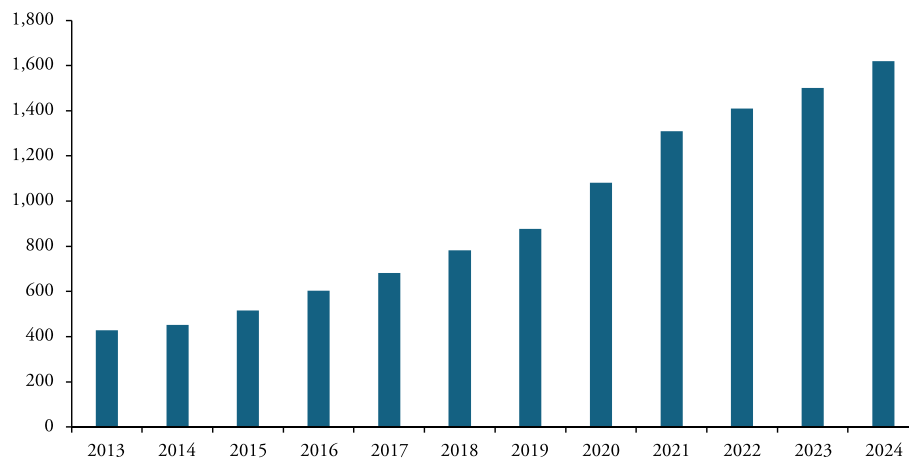
### **Conclusion**

The private credit sector is unlikely to collapse in a systemic event, though it would be economically meaningful. Private credit remains relatively contained within the larger financial system, with less reliance on short-term funding.<sup>20</sup> Moreover, risks are expected to emerge slowly and indirectly.

The most plausible scenario is a gradual tightening of credit conditions. Lending will slow as funds manage redemptions and reassess risk. Refinancing becomes more difficult for leveraged borrowers. There will likely be a heightened focus on certain sectors, software, other AI-exposed sectors, and insurance. The cumulative effect could weigh on investment and employment over multiple years, especially in Europe, where structural features may amplify adjustment dynamics.

Even if the “cockroaches” remain contained, their presence may still matter. The cumulative effect could be a sustained headwind to growth, especially in Europe, where structural features may amplify adjustment dynamics.

EXHIBIT 1.0 – GROWTH IN THE PRIVATE CREDIT MARKET, 2014-2024 (USD BILLIONS)



Source: UBS Asset Management.

## Notes

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- <sup>1</sup> <https://flow.db.com/topics/trust-and-securities-services/private-credit-a-rising-asset-class-explained#:~:text=Private%20credit%20is%20non%2Dbank,of%20lenders%2C%20and%20the%20borrower.>
- <sup>2</sup> [https://www.goldmansachs.com/pdfs/insights/goldman-sachs-research/cracks-in-private-credit/TOM\\_private%20credit\\_Redacted.pdf](https://www.goldmansachs.com/pdfs/insights/goldman-sachs-research/cracks-in-private-credit/TOM_private%20credit_Redacted.pdf)
- <sup>3</sup> <https://www.nytimes.com/2026/03/14/business/private-credit-jamie-dimon-cockroaches.html>
- <sup>4</sup> <https://www.ft.com/content/520dd246-89a6-4902-9a76-26b54adc91e9>
- <sup>5</sup> *Ibid.*
- <sup>6</sup> <https://www.funcas.es/wp-content/uploads/2026/02/8-Cuadros-15-1-1.pdf>
- <sup>7</sup> [https://www.goldmansachs.com/pdfs/insights/goldman-sachs-research/cracks-in-private-credit/TOM\\_private%20credit\\_Redacted.pdf](https://www.goldmansachs.com/pdfs/insights/goldman-sachs-research/cracks-in-private-credit/TOM_private%20credit_Redacted.pdf)
- <sup>8</sup> <https://www.bloomberg.com/news/articles/2026-03-26/trapped-in-private-credit-investors-wait-to-pull-out-5-billion>
- <sup>9</sup> <https://www.ft.com/content/520dd246-89a6-4902-9a76-26b54adc91e9>
- <sup>10</sup> <https://www.reuters.com/legal/transactional/private-credit-funds-shares-trade-steep-discounts-concerns-grow-2026-04-22/>
- <sup>11</sup> <https://www.ft.com/content/520dd246-89a6-4902-9a76-26b54adc91e9>
- <sup>12</sup> <https://www.ft.com/content/47606fe2-108e-4a71-ba2b-9e1b779edda8?syn-25a6b1a6=1>
- <sup>13</sup> <https://www.ft.com/content/520dd246-89a6-4902-9a76-26b54adc91e9>
- <sup>14</sup> [https://www.morganstanley.com/im/es-es/intermediary-investor/insights/articles/investing-in-european-private-credit.html#:~:text=European%20private%20credit%20AUM%2C%202013%2D2023%20\(\\$%20billion\),-DISPLAY%201&text=DISPLAY%201-,Source:%20Preqin%20data.,Private%20Credit%20to%20their%20portfolios.](https://www.morganstanley.com/im/es-es/intermediary-investor/insights/articles/investing-in-european-private-credit.html#:~:text=European%20private%20credit%20AUM%2C%202013%2D2023%20($%20billion),-DISPLAY%201&text=DISPLAY%201-,Source:%20Preqin%20data.,Private%20Credit%20to%20their%20portfolios.)
- <sup>15</sup> [https://www.europarl.europa.eu/RegData/etudes/STUD/2025/775947/IUST\\_STU\(2025\)775947\\_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/STUD/2025/775947/IUST_STU(2025)775947_EN.pdf)
- <sup>16</sup> *Ibid.*
- <sup>17</sup> [https://finance.ec.europa.eu/regulation-and-supervision/savings-and-investments-union/factsheet-breaking-down-barriers-integrate-financial-markets\\_en](https://finance.ec.europa.eu/regulation-and-supervision/savings-and-investments-union/factsheet-breaking-down-barriers-integrate-financial-markets_en)
- <sup>18</sup> <https://www.reuters.com/legal/transactional/ecb-sees-private-credit-risk-financial-stability-de-guindos-says-2026-04-21>
- <sup>19</sup> <https://www.aresgmt.com/news-views/perspectives/has-private-credit-been-tested#:~:text=Private%20credit's%20counter%2Dcyclical%20lending,financing%20evaporates%20during%20economic%20disruptions.>
- <sup>20</sup> [https://www.goldmansachs.com/pdfs/insights/goldman-sachs-research/cracks-in-private-credit/TOM\\_private%20credit\\_Redacted.pdf](https://www.goldmansachs.com/pdfs/insights/goldman-sachs-research/cracks-in-private-credit/TOM_private%20credit_Redacted.pdf)