



PRIVATE EQUITY ADVISORY – 2026 Q1

Private Equity *Market Update*

M&A MARKET PERSPECTIVE:

A Market Under Pressure, Not Paused

DEAL METRICS UPDATE:

Q1 2026 By The Numbers

A Market Under Pressure, Not Paused

We entered 2026 with a constructive outlook and many of the same optimistic signals we saw a year ago - momentum building out of the prior quarter, improving confidence, and the belief that deal and exit activity were poised to accelerate as market conditions improved.

One quarter in, the environment is starting to feel familiar – albeit for different reasons.

Geopolitical instability has reintroduced volatility into energy markets and inflation expectations, while growing scrutiny around AI disruption - particularly across software - is challenging broader assumptions around future growth and durability. Unlike this time last year, these factors have not stalled activity, but uncertainty has reemerged, resulting in more measured decision-making.

In Q4, we highlighted the middle market's ability to adapt amid persistent macroeconomic and geopolitical uncertainty. That same adaptability remains critical in today's environment.

This quarter, we explore how these dynamics are driving a widening valuation gap, reshaping how risk is underwritten, and increasingly flowing through to credit markets.

THE RETURN OF THE VALUATION GAP

Deal activity remains steady, but momentum is tempered - volatility and heightened buyer scrutiny, coupled with macro-driven uncertainty, have widened valuation expectations and raised the bar. Processes are still running, assets are being marketed, and capital remains available, yet fewer transactions are converting to close as buyers and sellers struggle to bridge the valuation gap.

Sellers, in many cases, remain anchored to valuations established in a fundamentally different environment and are not yet prepared to fully realize write-downs to meet current market levels. While improving sentiment and declining interest rates in 2025 helped narrow the gap, the underlying framework for assessing value has shifted. The past several years introduced meaningful distortions - driven by COVID

disruption, inflation, and supply chain volatility - making historical performance a less reliable indicator of future results. Even when those factors are normalized, sellers are increasingly required to address forward-looking uncertainties, including the potential impact of sustained geopolitical cost pressures and the evolving influence of AI on business models.

This dynamic is most visible in the exit environment, where activity remains somewhat muted and outcomes are dictated by pricing alignment. Notably, this persists even as many middle market companies continue to report relatively strong underlying operating performance and internal confidence. The gap is not just a pricing issue, it reflects a broader recalibration in how buyers underwrite risk, durability, and future earnings potential.

RISK REPRICING

Overlaying the valuation disconnect is a broader repricing of risk. Geopolitical instability driven by the prolonged conflict in the Middle East has elevated concerns around energy costs, brought inflation back into the narrative, and squashed the near-term potential for rate decreases. As a result, buyers and lenders are placing increased scrutiny on cost structures, margin durability, and overall earnings visibility.

At the same time, Q1 marked a shift in how AI-related disruption is being evaluated. The so-called "SaaS-pocalypse" highlighted a rapid increase in concern around the durability of traditional software models, with implications extending across industries as buyers and lenders reassess revenue quality, competitive positioning, and long-term growth assumptions.

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A Market Under Pressure, Not Paused

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Together, these forces are driving a more cautious approach to risk, narrowing the range of outcomes the market is willing to underwrite and setting the stage for tighter capital conditions.

CREDIT AS A FORCING FUNCTION

The repricing of risk is now flowing through to the credit markets. Assets acquired at peak valuations in 2021, particularly across software, are now aging into a financing environment that is materially more selective. With spreads widening and lenders tightening around structure and leverage, the ability to refinance rather than exit is no longer assured.

Recent signals from the private credit market reinforce this shift. Investor redemption requests and increased scrutiny around credit quality suggest that what was once a highly accommodative source of capital is becoming more constrained. Lenders are responding with greater selectivity, tightening underwriting standards and placing increased focus on downside protection and asset durability.

At the same time, capital is beginning to reallocate toward areas with more predictable performance and lower exposure to disruption. The recent increase in investment in Heavy-Asset, Lower-Obsolescence (referred to as "HALO") businesses is a clear example, as investors prioritize assets with tangible infrastructure, more stable cash flows, and limited downside exposure to AI-driven disruption. This shift reflects private equity's ability to assess changing market conditions, adapt its focus, and continue deploying capital in areas where risk-adjusted opportunities remain compelling.

Taken together, these credit market dynamics could act as a forcing mechanism. For several years, sponsors have largely avoided realizing losses, supported by accommodative credit and continuation vehicles. As refinancing options narrow,

GPs may be forced to confront the valuation gap that has constrained exit activity. While potentially painful in the near term, this may be the push needed to restore equilibrium across the private equity market.


LOOKING AHEAD: PROGRESS REQUIRES PRESSURE

The current environment reflects a market in transition rather than contraction. While valuation gaps, tighter credit conditions, and elevated risk scrutiny continue to constrain near-term activity, these same pressures are beginning to reset expectations and reestablish discipline across the market.

Importantly, activity within the middle market tells a more constructive story. Increased add-on activity, continued deployment of capital, and steady fundraising (albeit significantly concentrated with larger funds) signals indicate that sponsors are not retreating, but instead adapting – leaning into smaller, more actionable opportunities where conviction remains high and execution risk is more manageable.

While near-term constraints remain, continued activity and operational adaptability in the middle market may help sustain deal flow and provide a foundation for recovery as valuation expectations and capital markets begin to realign.



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Movement, but not Advancement

Q4 2025 wrapped up with deal value that rivaled the highs of 2021 (albeit with far fewer transactions), highlighting momentum driven by deal size, not volume. Against the backdrop of risk repricing in Q1 2026, deal volume moved up (5% QoQ and 6% YoY), but the impact of risk aversion was evident in deal value, which declined 18% QoQ and 7% YoY. ***In hindsight, the second half of 2025 looks like a bright spot amid continued challenges in the broader recovery.***

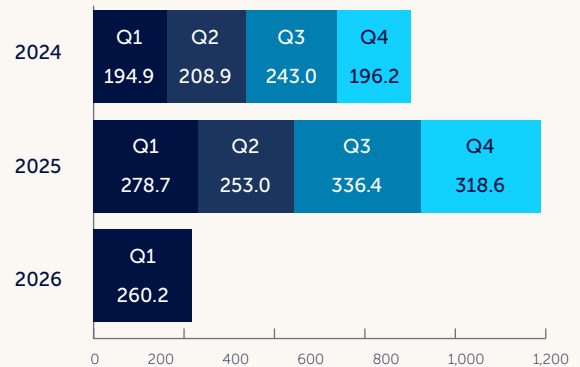
The “risk on” mindset that supported a stronger finish to 2025 reversed in early 2026, driven by concerns around AI’s impact on software investments and broader geopolitical uncertainty. Stable deal volume reinforces that sponsors remain active and continue to put capital to work, even as risk appetite shifts. However, the decline in value underscores a move down-market, where investors go to deploy capital in a more conservative manner. Nothing illustrates this more clearly than the rise in add-ons as a percentage of PE buyouts, reaching 76% in Q1, a level not seen since Q1 2023. Add-ons remain the ‘ol reliable’ for capital deployment when other avenues lack viability. While this mix is expected to rebalance as financing conditions improve and risk appetite returns, this is not that time.

Recession expectations rose to 45% in April (up from 35% in March) according to Goldman Sachs, reinforcing a more cautious market backdrop. This shift is further supported by more selective credit conditions, as lenders tighten around leverage and structure. Unlike the stark halt of activity after “Liberation Day” in Q2 2025, GPs are still deploying capital but doing so more selectively – favoring lower-risk opportunities that align with the more cautious underwriting approach.

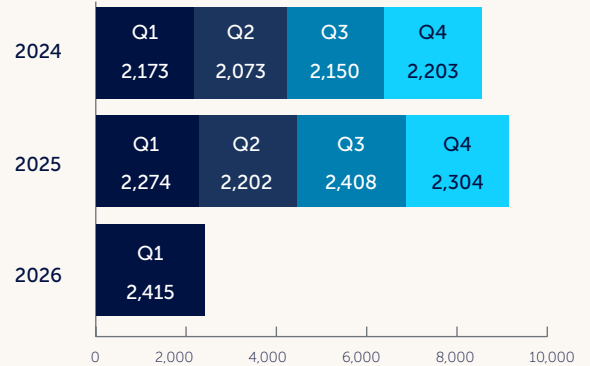
While deal activity remains steady, recapturing momentum will depend on narrowing the valuation gap and restoring liquidity through a sustained recovery in exit activity.

QUARTERLY PE DEAL ACTIVITY

DEAL VALUE (\$B)

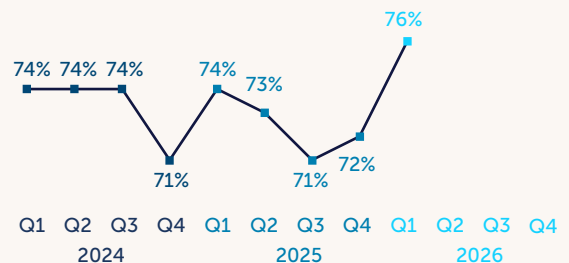


DEAL COUNT (#)



QUARTERLY PE ADD-ON ACTIVITY

% OF DEAL COUNT



Source: Pitchbook Data, Inc., US PE Breakdown

The Frailty of Exits

After positive exit trends to finish out Q4 2025, Q1 2026 took the wind out of the sails. Estimated exit activity totaled \$144B across 370 exits, down 17% and 33% QoQ, respectively. **Middle market exits trended in parallel, with an estimated 167 exits valued at \$30B, declines of 41% and 28% QoQ, respectively.**

Exit activity remains concentrated in high-quality assets, while those constrained by persistent valuation gaps remain in inventory.

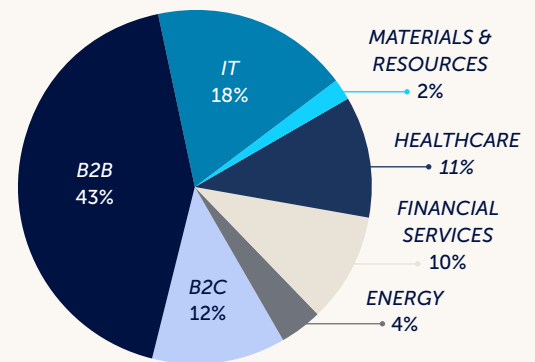
US private equity inventory continues to grow, reaching 13,325 companies in Q1, or roughly 8.7 years of backlog at the current pace of exits. Median hold times have continued to climb, surpassing four years – the record set last quarter.

Middle market fundraising finished 21% higher in Q1 2026 versus Q1 2025, while overall fundraising declined 4% YoY. This shift reflects the focus on down-market capital deployment.

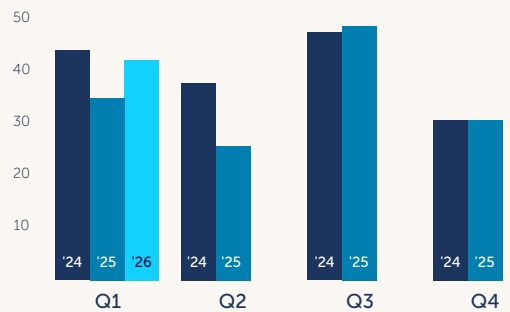
The fundraising concentration highlighted in Q4 2025 persisted into 2026, with the ten largest funds raising nearly 64% of total Q1 2026 capital. Amid concerns around overvalued portfolios and the slow return of capital to investors, LPs continue to concentrate capital with managers viewed as more reliable allocators in an uncertain market. Regardless of where capital is raised, without a meaningful increase in exit activity to work through the backlog of inventory, fundraising is expected to remain constrained.

As highlighted in previous quarters, a lack of exits has not halted deal activity, as GPs continue to work through significant dry powder. However, managers are now navigating a more complex environment marked by renewed valuation pressure, softening investor sentiment, and persistent macro-driven volatility. With an extensive backlog of aging assets, the path to liquidity remains uncertain, and optimism around a sustained exit recovery remains limited.

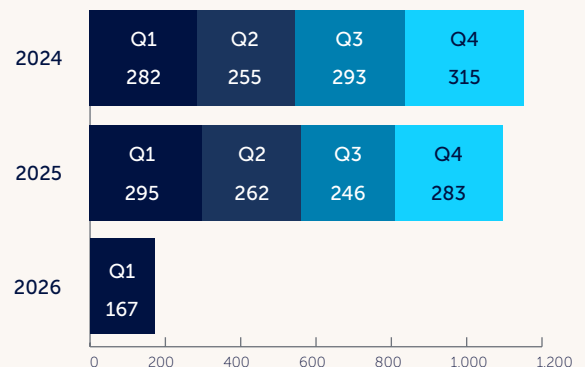
QUARTERLY PE DEALS BY SECTOR (#)



QUARTERLY PE MIDDLE MARKET ACTIVITY
MIDDLE MARKET FUNDRAISING (\$B)



MIDDLE MARKET EXITS (#)



Source: Pitchbook Data, Inc., US PE Breakdown



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- Tax Due Diligence
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- Merger Integration
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