

Private Markets Essentials



Private Markets Spotlight: Rate Cuts Boost Outlook for Private Markets

Key Takeaways

- » As widely expected, the Federal Reserve (Fed) announced a 25bps rate cut at its September 17, 2025 meeting and its projections anticipate another two 25bps cuts this year, for a total of 75bps by year-end
- » The anticipated series of rate cuts boosts our outlook for private markets as we see three ways in which rate cuts positively impact our asset classes
 1. Rate cuts should lower the cost of financing allowing for greater use of leverage
 2. Boost valuations of assets given the lower discount rate
 3. Make new transaction economics more attractive, helping boost overall investment activity
- » **Private Equity** should see a step-up in transaction and exit activity, as a result of rate cuts
- » **Private Credit** likely to benefit from lower interest expenses, higher debt service coverage ratios, and improvement in M&A activity
- » **Private Infrastructure** poised for an upside to valuations as well as potential inflation-linked upside to cash flows
- » **Real Estate** valuations, which lagged while other classes rebounded, could be further supported as yields and cap rates fall
- » **Royalties** as a broad asset class should benefit from the cheaper cost of leverage

The benefits of the upcoming rate cuts are visible and tangible across a variety of private market asset classes.

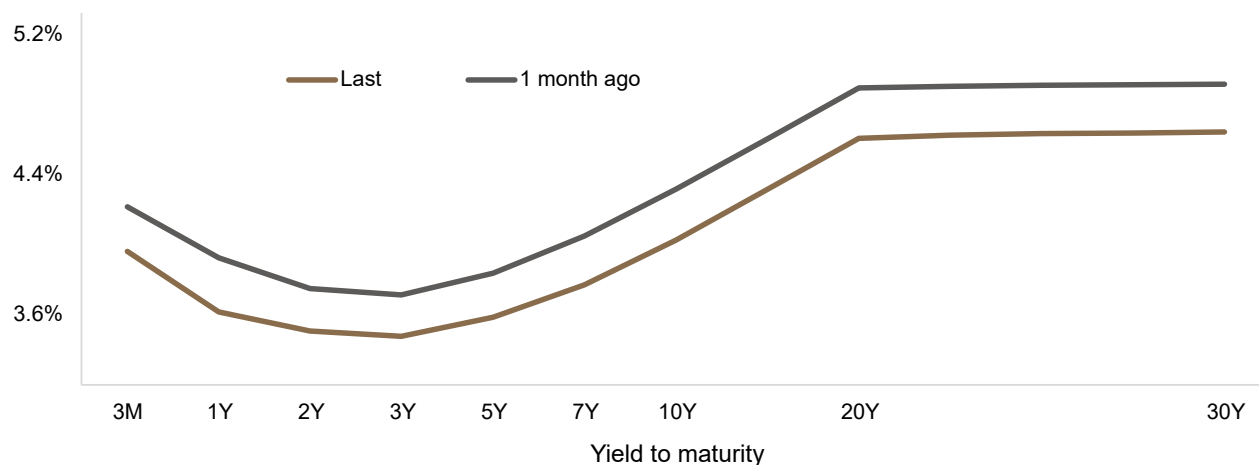
Overview

As widely expected, the Federal Reserve announced a 25bps rate cut at its meeting this week. During the press conference Fed Chair Powell also pointed out that the aggregate path of rate cuts, anticipated by the markets and its own committee projections which sees two more rate cuts this year, may provide additional support to the weakening labor market. The total of 75bps cuts is designed to serve as a “risk management” tool since the balance of risks has shifted.

The read-throughs from this resumption of the Fed's rate cutting cycle are clearly positive for public markets – although the S&P 500 was lower on the day of the Federal Open Market Committee (FOMC) announcement and bond yields rose, the S&P 500 is hovering near all-time-highs and the Treasury yields fell across the curve over the last few weeks. But what do these rate cuts mean for private markets? The anticipated series of rate cuts boosts our outlook for private markets as we see three ways in which rate cuts positively impact our asset classes.

Chart 1: Yields fell across the curve as markets priced in rate cuts this year

U.S. Treasury yield to maturity (YTM) by tenor



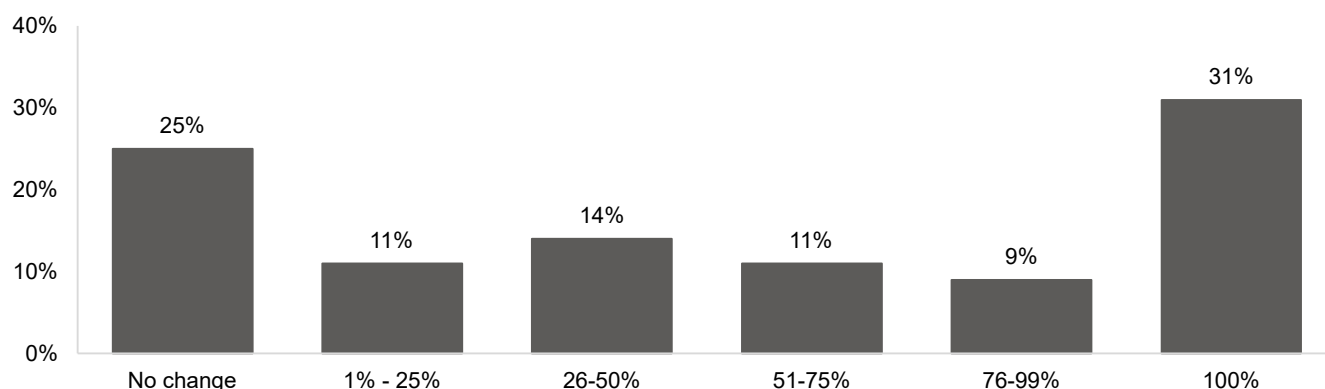
Source: Bloomberg (2025)

The labor market weakness prompted a September rate cut and we expect a few more

As noted by Fed Chair Powell, the U.S. jobs growth has slowed markedly in recent months, especially after accounting for the significant downward revisions. The signs of weakening are more and more apparent—the three-month average nonfarm payrolls growth is now running at just 29,000 per month, the number of job openings is below the number of unemployed people and is now below 1x for the first time since April 2021, and very few industries outside of healthcare are hiring at all. Powell also noted that a low hiring environment risks higher unemployment rate if layoffs begin to rise.

Of course, this slowdown makes sense—if companies' margins are under pressure due to tariffs as they have been for most of the year, they are likely to cut costs elsewhere and as a result, pause hiring. Indeed, one of the reasons why tariff passthroughs to consumer prices haven't been as significant as most economists expected is because companies have been absorbing much of the tariff increase.

Chart 2: Not all businesses plan to pass through tariff costs fully to consumers
Share of manufacturing businesses by percentage of tariffs cost they plan to pass through



Source: Partners Group, Federal Reserve of New York (2025). Surveys were conducted in May 2025. Since then, uncertainty around tariffs has moderated (e.g., transactions between the U.S. and Japan / Europe) which may result in firms seeing benefit in further margin squeeze to protect volumes rather than price on much of the import cost. For illustrative purposes only.

We expect the Fed to continue to support the U.S. labor market in the coming months because tariff-induced inflation is seen as a “one-off” and manageable, but labor weakness can develop and spread quickly. Additionally, what is inflationary now could quickly turn deflationary if the consumer pushes back when faced with labor market uncertainty.

The Fed is seemingly on track for two more rate cuts this year. Including this week’s rate cut, the ~ 75bps of easing could help cushion the labor market and the economy this year and into next. We think it is critical to do so at this juncture—as growth is slowing down due to tariffs but the tax cuts from One Big Beautiful Bill Act (OBBBA) have not yet kicked in.

Our outlook for the economy into 2026 is constructive, contingent on the Fed delivering these rate cuts. Assuming the Fed delivers, this is clearly a positive development—for the U.S. and global economy, for the stock market, and for our outlook for private markets.

We expect the positive impact of rate cuts to be threefold – 1) it lowers the cost of financing allowing for greater use of leverage, 2) it boosts valuations of assets given the lower discount rate, and 3) it makes new investment economics more attractive, helping boost transaction activity. These benefits should accrue to a variety of asset classes—private equity, private credit, infrastructure, real estate, and royalties. Here are the specific implications for each of these.

Private Equity

Should see a further step-up in transaction and exit activity, as a result of rate cuts

As interest rates fall across the curve, the cost of financing a buyout transaction declines, which in turn improves the acquired company financials, allows for greater use of leverage, and improves the probability of success and potential return on investment.

Lower cost of borrowing for private equity-backed companies using floating rate debt instruments also improves cash flows, which can then be used to invest in growth or returned to investors. It can also make additional financings cheaper, supporting the financing of capex projects and/or add-on acquisitions.

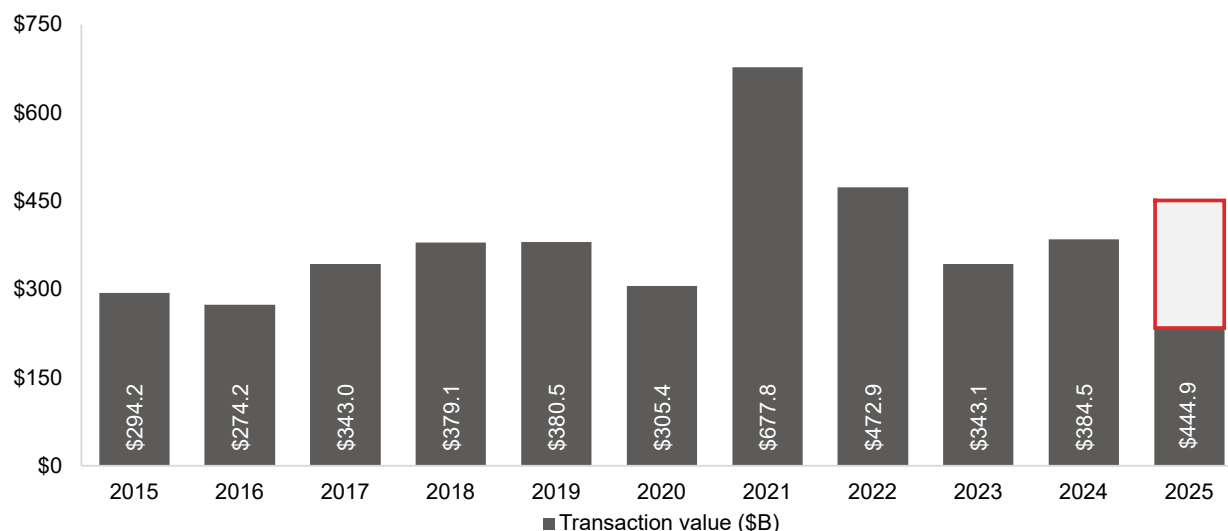
An increase in a company’s expected bottom line due to lower interest costs can also support higher valuations, especially as these greater cash flows are also discounted at a lower rate. Note that in addition to front-end yields, we have also seen yields decline in the belly of the curve—the 5-year and 7-year U.S. Treasury yields—which is important for transactions done with that holding time horizon in mind.

Finally, the indirect positive impact stems from the fact that lower base rates can also support the overall economic activity, including consumer spend and corporate expenditures, which in turn could lead to growth in revenues and EBITDA¹ for portfolio companies.

Together, all of these developments should increase the overall transaction activity in the private equity industry—as sellers are more comfortable with selling at a higher valuation while buyers are more comfortable with transaction fundamentals and can take advantage of lower cost of financing acquisitions. Indeed, we have seen U.S. buyout volumes rise +17% YoY in H1 2025², and we would expect these to rebound further.

Chart 3: U.S. activity is on pace for a strong rebound from 2024 levels

Private equity buyout transaction volumes for the U.S.

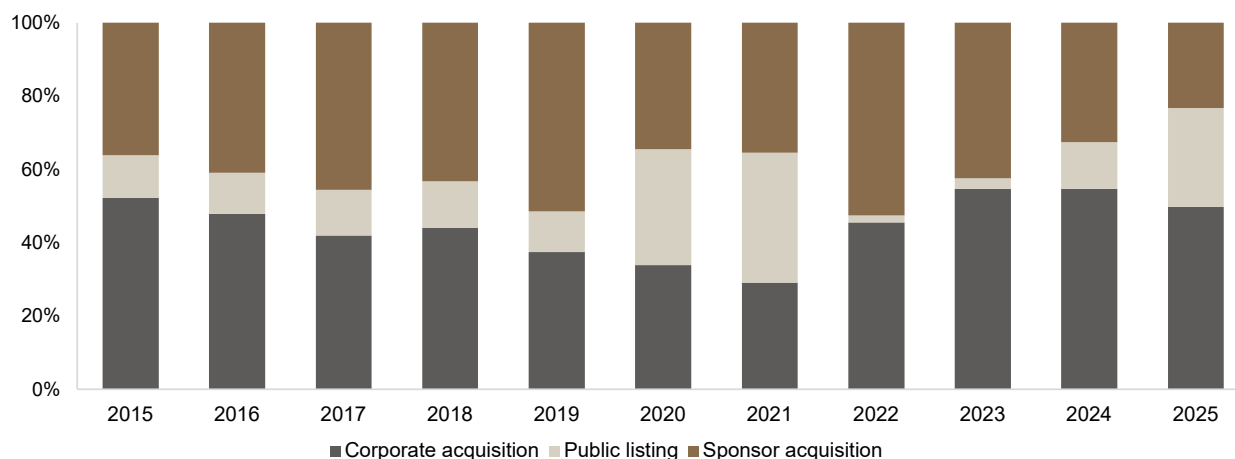


Source: PitchBook (June 2025). Red box denotes projected H2 2025 U.S. buyout activity assuming the same volume as in H1 2025.

Exit activity should also benefit, as a result of rate cuts. So far this year global M&A volumes are up +25% YoY³ and global IPOs are up +27% YoY². The valuation support from the upcoming rate cuts (which similarly accrue to public markets) combined with greater clarity on trade, and the strong Initial Public Offering (IPO) performance year-to-date (YTD) should continue to drive robust IPO activity over the course of the rest of the year. Assuming the robust Q3 25 pace carries over into Q4 25, we could be on track for the best year of IPO volumes since 2021 and closer to pre-COVID levels. Notably, public listings represent an increasingly important venue for private equity exits this year—the highest percentage since 2021.

Chart 4: IPOs have been a major source of private equity exits in 2025

Share of U.S. private equity exits by type



Source: PitchBook as of June 2025

Private Credit

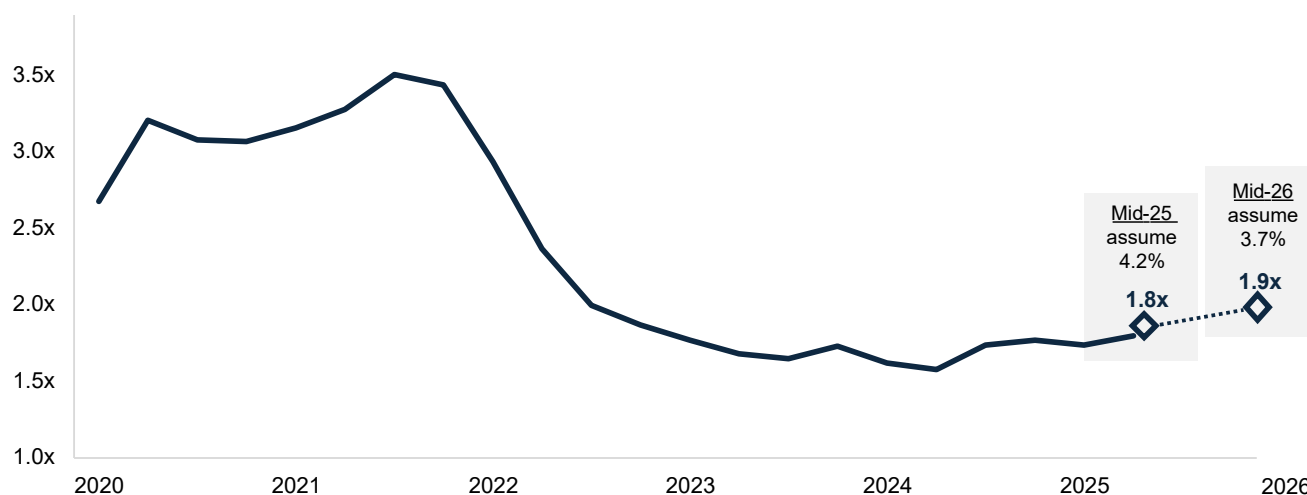
Likely to benefit from lower interest expenses, higher debt service coverage ratios, and improvement in M&A

Given the floating rate nature of the loans (most typically tied to a 3-month term Secured Overnight Financing Rate Data (SOFR)), rate cuts would have an immediate positive impact on borrowers' debt servicing costs. This impact hasn't yet been felt but could quickly take effect after the cuts materialize. This could alleviate the financial burden on the borrowers and put them in stronger liquidity positions, while also helping alleviate investors' concerns about default risk. Additionally, while there has been an increase in payment-in-kind (PIK) interest in the market in recent quarters, lower rates/higher borrower liquidity could help to reverse that trend.

Finally, if a company spends less on interest expenses, it can free up cash flow to use it for other needs—offsetting the cost of tariffs or investing in capex or payroll expenses, and thereby, improving growth prospects.

Chart 5: The interest coverage ratios have troughed and are gradually improving

Average interest coverage ratios



Source: Houlihan Lokey (Aug 2025). Interest coverage ratio is defined as adjusted EBITDA divided by total interest expense using the Houlihan Lokey Private Performing Credit Index (PPCI). There is no guarantee that targets will be met, and actual results may differ materially.

Private credit can further benefit from the expected increase in M&A activity and direct lending transaction volumes. As detailed previously, lower cost of debt would likely lead to a pick-up in M&A activity, increasing the supply of direct lending transactions in the market.

Further, U.S. leverage ratios declined as rates rose, but this trend could also reverse with the share of leverage used in transactions reverting to higher levels increasing the opportunities for private credit lenders. We could see potentially modest upward momentum in spreads—since the increase in transaction supply could encourage modest spread widening. This move could partially offset the decrease in base rates, helping to keep all-in private credit yields attractive.

Private Infrastructure

Is poised to see an upside to valuations as well as potential inflation-linked upside to cash flows

Like private equity, infrastructure assets should benefit from lower financing costs and higher discounted cash flow (DCF) valuation, as a result of lower rates, but with one important caveat—long-term rates tend to be more impactful for infrastructure asset valuation than short term rates. Importantly, we did see the 10-year U.S. Treasury yields decline in recent weeks—partially due to lower growth and greater rate cut expectations and partially because of the reduced concern about the U.S. budget deficits (as a result of tariff revenue) and Fed independence.

Another aspect to consider for infrastructure investors is the potential change in inflation as a result of these rate cuts. Most infrastructure assets have an implicit or explicit link to inflation through regulatory tariffs or contractual structures (or at least the ability to pass through inflation) and, as such, provide investors protection in an inflationary environment.

While it is not certain if rate cuts will lead to higher inflation, there is that risk—since rate cuts could support stronger growth, asset inflation, provide stimulus for consumers as credit costs fall, spur weaker dollar and therefore, potentially higher import costs. As a result, infrastructure should continue to be top of mind for investors—as a hedge against firmer-than-expected inflation and as a continued beneficiary of secular growth in power generation and digitization, as well as the cycle of upgrades required for aging assets.

Real Estate

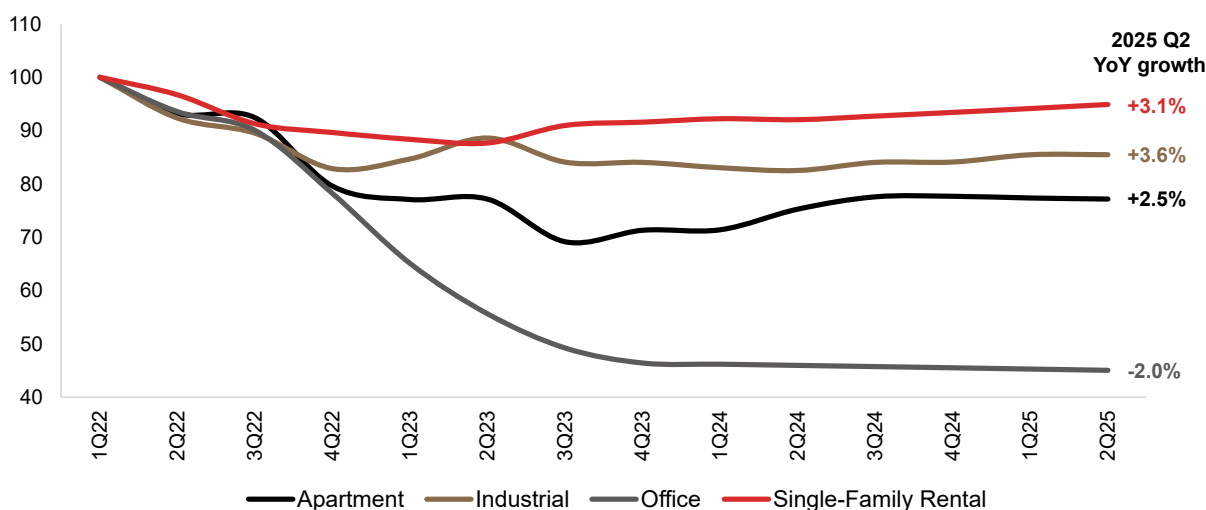
Valuations which lagged, could be supported as yields and cap rates fall

Much like other asset classes, real estate stands to benefit from the lower cost of financing and with it, likely higher transaction volumes. However, unlike other asset classes, real estate valuations are yet to materially recover. For example, cap rates have stagnated at around 6.5%⁴ and property prices are still -12.2% below their Q2 22 peak⁴.

As U.S. Treasury yields decline across the curve with rate cuts, we would also expect to see the cap rates to come in as most real estate sector fundamentals are healthy (outside of office). This should support the price recovery of real estate. There is one caveat to note—the Fed's success in propping up the labor markets will be key to ensuring that the rent growth prospects do not weaken.

Chart 6: Property prices have stabilized, though are still well off the peak

Green Street U.S. commercial property price index



Source: Green Street (June 2025).

Royalties

Should benefit from the cheaper cost of leverage

Royalties is a sizable and growing asset class, providing investors resilient and uncorrelated yield, where as a royalty investor, you hold the right to receive a share of the revenue generated from the assets that you own, which could come, for example, from the sale of a pharmaceutical drug, gold extracted from a mine, or the ongoing use of a musician's song catalog. This asset class should also see a positive impact from rate cuts. Leverage used in royalties' investments includes senior bank loans based on term SOFR rates + 200-300bps spread, and much like for private credit, these loans should see immediate declines in interest costs as rate cuts materialize. Longer-term, cheaper leverage may also lead to an increase in royalty valuations.

In conclusion, the recent and anticipated further Fed actions clearly boost our outlook for private markets. The benefits of the upcoming rate cuts are visible and tangible across a variety of private market asset classes and across our platform.

Footnotes

¹ Earnings Before Interest, Taxes, Depreciation, and Amortization

² Source: PitchBook as of June 2025

³ Source: Dealogic as of September 2025

⁴ Source: MSCI Real Capital Analytics as of June 2025

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