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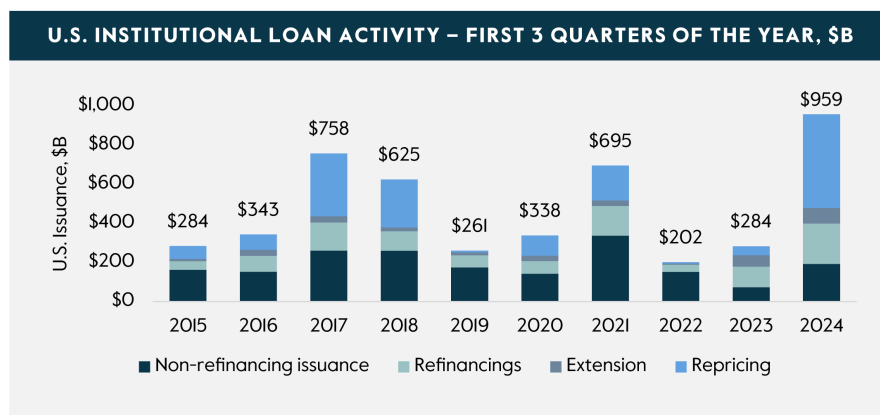
By **Hannah Khizgilov**
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Welcome back to **The Carlyle Compass**, your weekly newsletter that brings together the latest research and market insights from our global team. This week's edition features guest author Hannah Khizgilov, Vice President in Global Research & Investment Strategy, and highlights key takeaways from AlInvest's Global Private Markets Quarterly.

Record Leveraged Finance Issuance

Though the U.S. Federal Reserve was not the first central bank to cut rates this cycle, its 50 basis point cut in September was the clearest sign that we've entered a new global monetary policy regime. Investor sentiment continues to improve as market participants assess that base rates have further to fall from here. That sense of optimism has been evident in the leveraged loan market, where spreads compressed to post-2008 lows as demand—driven entirely by still robust CLO issuance (net loan fund flows turned negative in the quarter)—continued to outpace supply. When including high-yield bonds, full-year leveraged finance issuance seems likely to exceed \$1 trillion for only the third time in history (Figure I).

Figure 1: Record Institutional Loan Activity



Source: Pitchbook/LCD accessed 10/7/24. There is no guarantee any trends will continue.

The main driver of this year's record-breaking issuance is, as is well known among market participants by now, the boom in refinancing and repricing transactions. Historic spread tightening has meant that speculative grade borrowers could meaningfully reduce their financing costs despite the highest level of base rates in two decades. Through the first three quarters, U.S. refinancing and repricing volumes totaled a record-breaking \$686 billion and made up 72% of all institutional loan activity.

At this stage of the game, there are few performing loans left to refi or reprice. At roughly \$30 billion, U.S. loan refinancings in Q3 fell nearly 70% relative to Q2 and are now running below the quarterly average in all of 2023. Repricing activity also slowed in Q3, involving just \$101 billion of loans in Q3, a notable step down from the record-breaking \$224 billion in Q2 and \$155 billion in Q1.

Thankfully, new supply appears ready to fill the void. In the U.S., new-issue loan volume tied to LBOs and related add-ons reached the highest level in two-and-a-half years. Non-refinancing activity—proceeds used for M&A, capex, or general corporate purposes—exceeded a third of total issuance for the first time since the second quarter of 2022. Base rates are falling and investors seem ready to put money to work in response. 2024 has been a borrowers' market, but recent trends suggest supply and demand should move into better balance in the quarters ahead.

Reaping Dividends

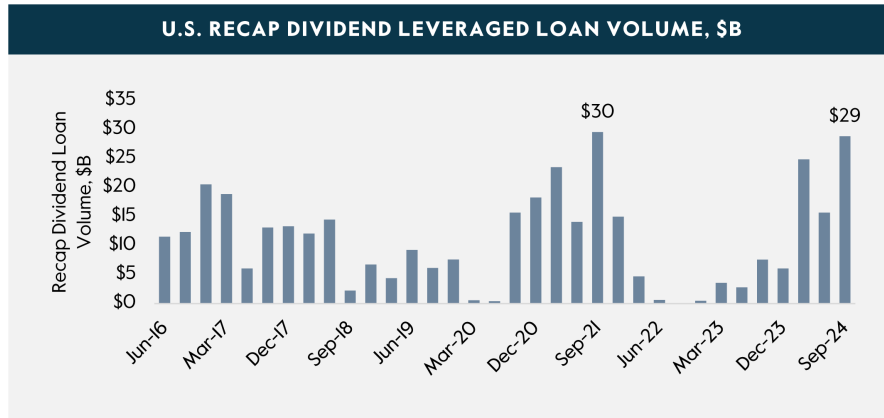
Easier financial conditions have not just reduced interest expense, but also allowed financial sponsors to send cash back to their LPs at a time when exit activity remains sluggish.

Though Initial Public Offerings (IPOs) get most of the attention, the majority of private equity-backed companies are exited through trade sales. And they've been relatively weak, as high base rates and strong organic earnings growth have left strategics content to sit on the sidelines. The rebound in M&A activity has been mostly a private equity phenomenon. In the third quarter of 2024, GPs announced global LBO transactions totaling approximately \$150bn (including add-ons), an eye-popping 42% increase year-on-year. Through the first nine months of 2024, financial sponsors have accounted for 18% of global M&A volumes, 50% higher than the post-GFC average.

The decline in trade sales has delivered a negative liquidity shock to private markets. Capital calls (cash outflows) exceeded gross distributions (cash inflows) for limited partners (LPs) in buyout funds for eight consecutive quarters, the longest stretch of net negative distributions since the Global Financial Crisis (GFC).

That's finally ended. Last quarter, gross distributions finally exceeded capital calls and the margin appears to be growing. This was mainly thanks to accommodative financing conditions. Sponsors took advantage of red-hot credit markets to issue the second-most (leveraged) dividends on record (Figure 2). Quarterly totals mask recent acceleration: September volumes alone totaled \$19.2 billion, the most for any month in the U.S. loan market by a wide margin. This was led by [consortium-backed Belron's blockbuster recapitalization deal](#), which is believed to be the largest such transaction of all time.

Figure 2: Dividend Recapitalizations Boost Liquidity



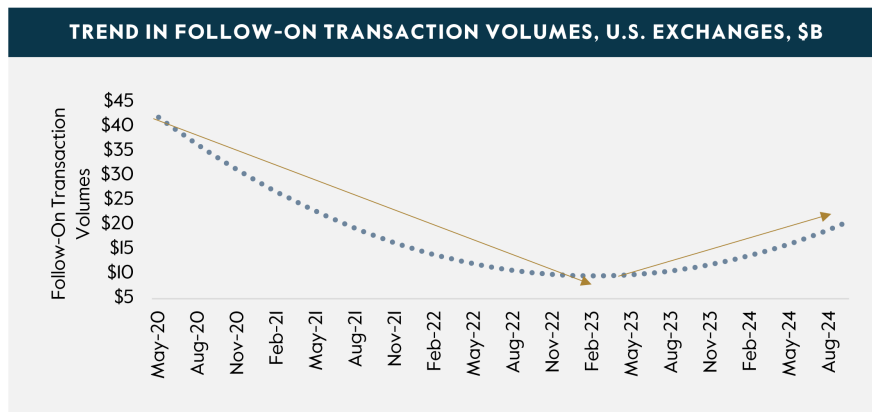
Source: Pitchbook/LCD accessed 10/7/24. There is no guarantee any trends will continue.

Trade sales should pick up in the coming quarters, as slowing revenue growth leads strategics to seek out accretive acquisitions to hit earnings per share (EPS) targets. But these data provide a reminder that sponsors can utilize other tools—including portfolio finance solutions and GP-led secondary transactions—to send some portion of unrealized portfolio value back to LPs in the meantime.

IPO Green Shoots

The effect of easier monetary policy is already evident in the U.S. IPO market. Excluding SPACs, 119 U.S. exchange-listed IPOs raised \$26.2 billion in the first nine months of the year. This is 30% more listings and a 50% increase in proceeds relative to the same period last year. While listing activity remains well below white hot 2021 levels, it is notable that follow-on transactions—often seen as a leading indicator for IPO sentiment—are [on the rise](#) (Figure 3). Sponsor-backed IPO activity in the fourth quarter is already off to a strong start, with the highly successful [oversubscribed offering of aircraft maintenance firm StandardAero](#).

Figure 3: Follow-On Transactions Can Signal IPO Thaw



Source: Dealogic, accessed 10/13/24. There is no guarantee any trends will continue.

Cross-border transactions play a significant role in the IPO recovery seen to date, as U.S. equity market liquidity remains unrivaled. (A fact many foreign investors in the Japanese stock market discovered to their dismay in early August). Since 2023, over half of U.S. IPOs have been from issuers domiciled outside of the States, marking a 20-year high. The third quarter also saw a resurgence of tech-related IPOs relative to Q2. 51% of transactions in Q3 were companies in IT and healthcare (biotech), sectors that, excluding AI, fell sharply out of favor as rates rose.

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