APOLLO

2026 Credit Outlook: From Scarcity to Selection—The Return of a Buyer's Market

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KEY TAKEAWAYS

- **Credit has shifted back into a buyer's market.** Economic growth in the US is expected to support corporate and consumer fundamentals in 2026. But the technical backdrop has flipped. After years of scarcity, credit markets are entering a higher-supply regime driven by AI-related hyperscaler issuance and a reacceleration in M&A. With IG yields near three-year lows and issuance volumes rising, clearing the market will increasingly require pricing adjustments, shifting the power back to lenders and creating a more favorable setup for buyers of credit.
- **AI is now the single largest source of incremental credit supply.** The AI investment cycle has evolved from a self-funded capex story into a broad-based financing event. Hyperscaler capex has already tripled since 2023 and sell-side forecasts point to more than $2.7 trillion of cumulative AI-related spending from 2025 to 2029. As internal cash flow struggles to keep pace with this rising investment, debt—across public IG, private credit, project finance, CRE, and ABS—will play a central role, reshaping issuance patterns, benchmarks, and correlations across credit markets.
- **AI issuance will increase concentration risk.** AI-related exposure is becoming pervasive across portfolios. What appears diversified across issuers and sectors increasingly represents a single macro trade on AI. This raises correlation risk and increases the value of diversification into areas structurally insulated from the AI arms race, including European private credit and sports financing.
- **M&A is returning at scale, reinforcing the supply backdrop.** The resurgence in M&A reflects a supportive alignment of lower financing costs, workable valuations, ample private equity dry powder, and a more supportive policy environment. As deal sizes grow, issuers are turning to more complex, multi-tranche capital structures that tap multiple pockets of the credit markets at once. The return of large-scale M&A can further expand credit supply in both IG and leveraged finance, reinforcing the buyer's market dynamic.
- **The cycle is defined by dispersion, not distress.** The defining macro feature of this cycle is not weak growth, but increasingly narrow growth. Economic strength is concentrating among higher-income consumers and large, AI-exposed corporates, while pressure builds across more rate- and income-sensitive households and businesses. This K-shaped dynamic is now evident across consumption, investment, and corporate fundamentals, driving wider dispersion within credit markets. Importantly, this is not a market defined by systemic stress or forced selling, but by selectivity, where dispersion is the mechanism through which attractive entry points emerge for disciplined buyers of credit.

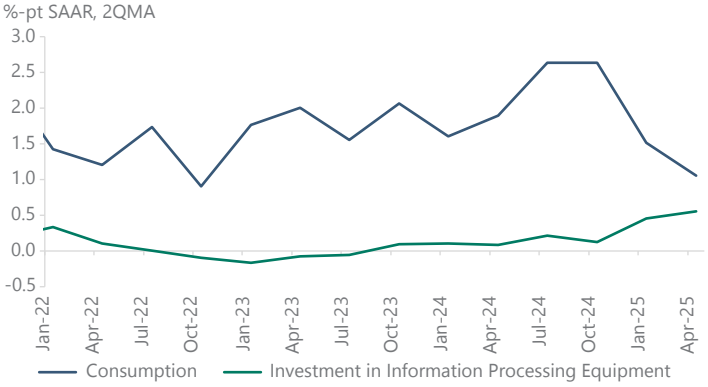
Introduction:

Last year, credit markets and the broader US economy once again confounded expectations. As we noted entering 2025 and reinforced at midyear, tariff-driven volatility, geopolitical flare-ups, and fiscal debates generated sharp but fleeting disruptions. Liberation Day marked the most acute test of the market's resilience, briefly exposing pockets of liquidity strain before policy moderation allowed risk markets to reassert themselves. In the second half of the year, attention increasingly shifted away from policy noise toward a more powerful underlying driver: a renewed surge in large-scale investment—most visibly tied to AI, digital, and data infrastructure—that began to shape capital allocation, financing needs and dispersion across credit markets.

That shift in focus was soon reflected in the economic data. A surge in AI-related investment and strong consumer spending helped offset early-year tariff shocks, driving better-than-consensus economic growth. Third-quarter gross domestic product (GDP) in the US expanded at a 4.3% annualized rate,[1] the fastest pace in two years. JPMorgan estimates that roughly one-third of first-half 2025 US GDP growth came from tech-driven business investment tied to AI infrastructure.[2] Data-center investment contributed almost as much to first-half GDP growth as consumer spending—an extraordinary shift given that consumption makes up roughly 70% of GDP and is typically the economy's main driver **(Exhibit 1)**. While aggregate fundamentals have remained resilient, economic growth has trended unevenly across sectors and income demographics, underscoring a distinctly K-shaped economy.

The robust macro backdrop has supported a broader earnings recovery. While the earnings and valuation gap between AI-linked leaders and the rest of the index continues to widen, the broader index surprised to the upside in the third quarter. Roughly two-thirds of S&P 500 companies delivered earnings beats (15% above their historical average[3]), and the median Russell 3000 stock saw about 8% year-over-year EPS growth, the strongest result in four years **(Exhibit 2)**.

Exhibit 1: Contribution to GDP Growth From Consumer Spending & Data Center Investments



Data as of Q2 2025.
Sources: US Bureau of Economic Analysis (BEA), Macrobond, Apollo Chief Economist

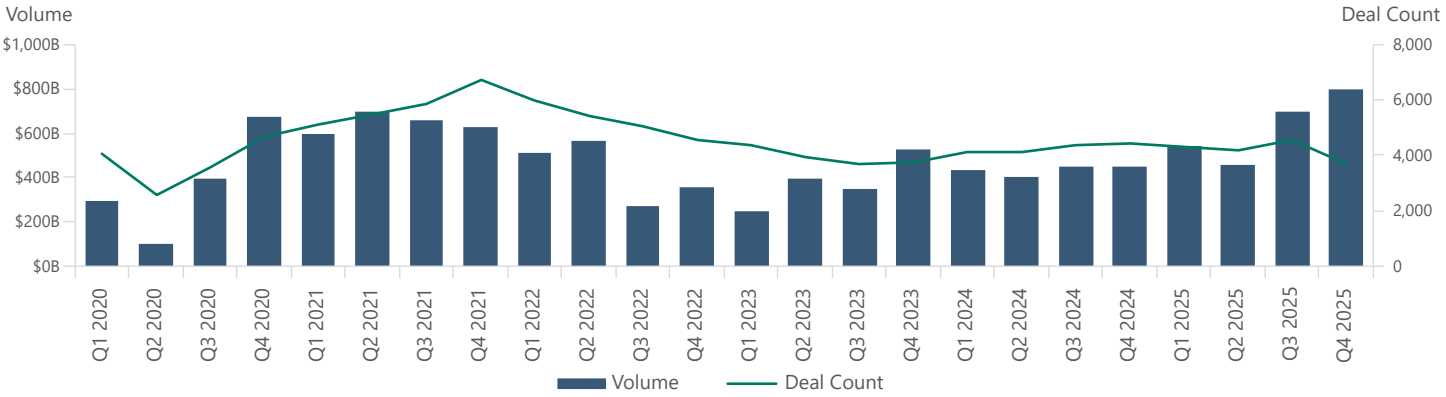
Exhibit 2: Frequency of S&P 500 Earnings Surprises

Data as of November 2025.
Source: Goldman Sachs Global Investment Research

Meanwhile, the long-expected M&A resurgence arrived in earnest in the summer, unleashing a broad pickup in strategic dealmaking. Corporate confidence strengthened as rates fell and antitrust enforcement eased, culminating in a wave of dealmaking across technology, communications, and consumer sectors. North American deal volume in 2025 rose to $2.4 trillion, the highest figure since 2021 and the second highest on record **(Exhibit 3)**.

[1] US Bureau of Economic Analysis, December 2025.
[2] JPMorgan, September 2025.
[3] Morgan Stanley, 2026 US Equities Outlook, November 2025.

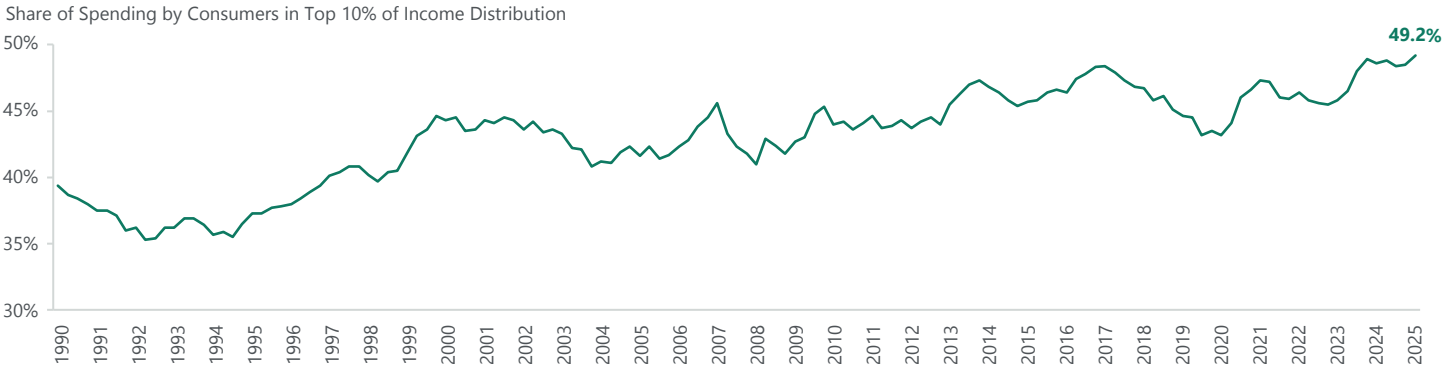
Exhibit 3: North American M&A Transactions



Note: Includes pending and completed deals, and one count of WBD transaction. Data as of December 2025. Source: Bloomberg

Despite robust top-down economic growth, its transmission has been uneven across sectors and income demographics, underscoring a distinctly K-shaped recovery. Consumption is increasingly concentrated among higher-income households, with the top 10% now driving nearly half of all consumer spending while the bottom 80% account for a shrinking share, leaving the expansion increasingly dependent on the top decile of consumers **(Exhibit 4)**.

Exhibit 4: K-Shaped US Consumption



Data as of June 2025.
Sources: Moody's, Federal Reserve

CREDIT MARKETS: FUNDAMENTALS ROBUST BUT TECHNICALS ARE WEAKENING

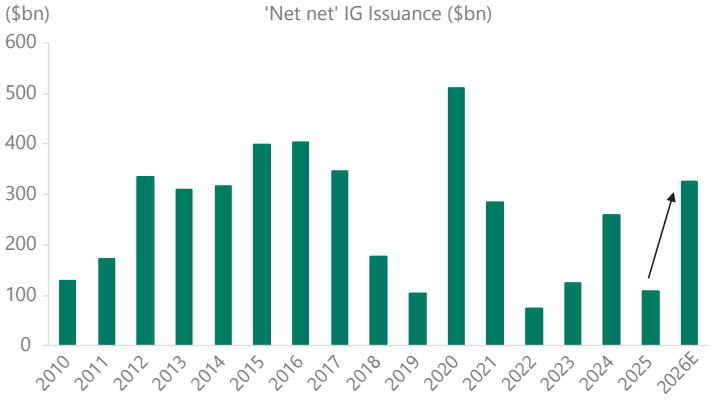
Credit fundamentals have held firm, supported by a strong macro backdrop. High yield (HY) issuers delivered revenue and EBITDA growth of 4% and 1.7%, respectively, in the first nine months of 2025.[4] The pressure on interest coverage ratios also eased as the Fed cut short-term rates by 75 basis points during the year. Further, strong credit technicals—tight net supply and steady institutional demand—kept both investment grade (IG) and HY markets well anchored, even as policy and geopolitical uncertainty persisted. That dynamic drove credit spreads to multi-decade tights, with IG touching a low of 72 basis points and HY at 260 basis points during 2025.[5]

As we enter 2026, we expect economic growth near 2% in the US,[6] which should be enough to sustain fundamentals for most corporate and consumer borrowers. However, the technical backdrop has flipped.

[4] JPMorgan, December 2025.
[5] ICE BofA US High Yield Index Option-Adjusted Spread.
[6] Bloomberg, December 2025.

However, the technical backdrop has flipped. After several years of scarcity, credit markets are transitioning into a higher-supply regime **(Exhibit 5)**, driven by rising hyperscaler issuance tied to AI-related capex and a reaccelerating M&A pipeline. While demand remains solid, with IG yields near three-year lows, we expect investors to require more meaningful new-issue pricing adjustments to clear elevated volumes, setting up what increasingly looks like a buyer's market in credit. Against that backdrop, borrowers—especially hyperscalers and financial and strategic sponsors—will increasingly look across markets to meet funding needs. We think this dynamic will favor a flexible investment mandate across public and private corporate and asset-backed finance (ABF) markets that can also source and structure complex bespoke financings. Across these asset classes, dispersion, structure and selectivity should define opportunity as markets adjust to a new supply regime.

Exhibit 5: Tight Net IG Supply



Data as of December 2025. Source: JPMorgan
'Net net' IG Issuance defined as IG net issuance minus coupons.

We see the following opportunities across major credit sectors:

- **In IG**, the surge in high-quality issuance is likely to push spreads wider and lift credit risk premia, especially in public IG, where levels remain historically tight. Further, correlation and concentration risk should increase significantly. Private markets should be better insulated given wider spreads, stronger covenant protection and a more diversified risk profile. In particular, flexible mandates that can invest across the full spectrum of IG risk—spanning both corporate and ABF—should offer diversification benefits that are increasingly scarce because of the AI concentration in public markets. Wider private IG spreads also help shield the asset class from a pickup in interest rate volatility.
- **In Leveraged Finance**, while BB spreads are historically tight, we believe they offer better risk/reward than BBBs given the former are less exposed to supply risk. Further down the quality spectrum, increasing dispersion is creating opportunities on both sides of the Atlantic. Dispersion in European HY has opened attractive entry points in some higher quality single Bs that have widened by roughly 100 basis points through November 2025. In the US, compressed loan spreads through the end of the year have made single-B HY relatively more appealing relative to loans on a risk-adjusted basis. Across regions, the most durable opportunities continue to cluster in higher quality, secured risk. Despite market concerns, we do not see broad structural risk in BDCs: liquidity remains ample and underlying asset quality is generally stable. Pricing on middle-market CLO tranches backed by similar collateral has remained relatively tight, even as unsecured BDC debt has traded wider, suggesting limited stress at the asset level. That said, as the BDC market matures, we expect greater differentiation among managers, driven primarily by disparities in credit performance.
- **In ABF**, we see a broadening set of opportunities: Europe's higher asset density and capital intensity—characterized by long-lived physical assets—create a natural fit for asset-backed financing at a time when regulatory shifts and strategic priorities in defense, technology, and energy transition are creating new funding demands. In addition, the rapid buildout of digital infrastructure in the US, particularly data centers, is opening up a new frontier as more of the AI investment cycle is financed with debt. Finally, the K-shaped consumer narrative has created a dispersion of opinions in the Consumer Finance sector, leading to selective investment opportunities. Across ABF pillars, we believe residential mortgages, commercial mortgages and capital solutions, especially NAV loans, provide the most attractive relative value in the near term, but expect a healthy pipeline across the entire business in 2026.

That said, while this is not our base case, there are two macro dynamics that warrant close monitoring in 2026 given their potential to disrupt an otherwise constructive backdrop for credit:

1. Inflation and rate volatility. Inflation has remained stubbornly elevated and harder to interpret in the wake of the government shutdown. The most recent readings have hovered around 3%, above the Fed's stated 2% target, with inflation increasingly broad-based. At the same time, labor market signals softened as 2025 progressed: layoffs at major employers picked up, private payroll gains slowed, and unemployment rose as labor force participation increased. Although the Fed has cut its target rate by 75 basis points over the past 12 months, the path forward for further rate cuts remains uncertain. Divergent inflation and labor market data, combined with the appointment of a new Fed chair in 2026, could inject meaningful uncertainty into monetary policy expectations, potentially driving rate volatility higher.

2. Concentration risk in AI-led growth. US growth has become increasingly dependent on AI-related investment, with recent gains in real private fixed investment driven almost entirely by information-processing equipment and data-center buildouts, while non-AI corporate capex has remained largely flat. At the same time, markets have become discriminating around the future ROI of AI investments, reinforcing the economy's exposure to any negative surprise in AI adoption or monetization. Should revenues ultimately fail to justify the scale of current spending and AI-related capex slow, the implications for growth and credit markets would be material; conversely, if returns exceed expectations, the likely response would be another step-function increase in capex and associated supply, intensifying the already challenging credit technicals in 2026.

Key Themes in 2026

We see three themes taking center stage in the year ahead:

- **Financing the AI Revolution:** AI has become the single largest source of incremental credit demand, with hyperscalers' expanding capex needs now driving issuance across IG, ABS, CRE, and project finance—creating cross-asset correlation risk and relative value opportunities.
- **The Return of the Megadeal:** Large-scale M&A is returning as cheap IG financing, ample private equity dry powder, and a more LBO-friendly corporate bond market open the door to bigger, more complex transactions.
- **K-Shaped Credit:** AI is turbocharging the divergence between higher- and lower-quality borrowers, producing a two-speed credit environment, deepening sector dispersion and creating attractive entry points for investors.

Theme 1: Financing the AI Revolution

In our 2025 Credit Outlook, we discussed the large financing requirements that would emerge alongside the AI-related data center buildout. Looking at our projected $2 trillion of spending on AI infrastructure through 2030, it's striking how modest that estimate now appears, with current projections approaching $5 trillion over the next five years.[7] This increase in investment scale and ambition carries with it a correspondingly large need for financing. What began as a contained, self-funded capex story among the five hyperscalers has transformed into a market-wide financing event, with its impact felt on credit benchmarks and issuance calendars, that has raised questions around concentration and correlation. While the jury is still out on whether we are in the formative years of a durable technology-led investment cycle or the early stages of an investment bubble (which are not necessarily mutually exclusive), the scale is no longer in dispute: AI is now the single largest source of incremental financing across public and private credit markets. From 2021 through 2024, banks were usually the largest source of supply, with tech issuers tapping the bond market intermittently and at a far smaller scale. In 2025, large AI-linked borrowers not only occupied multiple top 15 positions but collectively represented roughly $120 billion of the approximately $380 billion issued by this cohort of companies **(Exhibit 6).**

Exhibit 6: Top 15 Issuers Trending Away From Banks and Towards Tech, Media & Telecom

	2021		2022		2023		2024		2025	
	Issuer	Issuance $bn	Issuer	Issuance $bn	Issuer	Issuance $bn	Issuer	Issuance $bn	Issuer	Issuance $bn
1	GS	43.7	BAC	40.2	PFE	31.0	JPM	39.5	META + RPLDCI*	57.3
2	JPM	41.3	JPM	33.1	WFC	27.7	MS	35.8	MS	36.0
3	BAC	41.3	WBD	30.0	MS	26.3	C	30.7	C	35.9
4	MS	34.5	MS	26.0	BAC	25.0	GS	29.8	GS	26.4
5	VZ	26.0	C	25.3	AMGN	24.0	UNH	18.0	JPM	26.0
6	AER	22.0	WFC	23.5	JPM	18.0	WFC	16.8	MARS	26.0
7	AAPL	20.5	GS	23.2	HSBC	16.0	HSBC	16.5	ORCL	25.8
8	AMZN	18.5	AMZN	21.0	UBS	15.0	ABBV	15.0	HSBC	23.8
9	C	18.5	HSBC	18.5	C	13.5	RY	14.0	BAC	23.0
10	HSBC	16.5	TD	17.3	SUMIBK	13.4	CSCO	13.5	GOOGL	22.5
11	ORCL	15.0	UNH	15.0	PNC	12.0	TOYOTA	13.3	WFC	19.5
12	UBS	13.3	UBS	13.8	BACR	11.8	BMY	13.0	UBS	16.3
13	TOYOTA	12.6	CS	13.3	CVS	11.0	ANZ	12.8	AMZN	15.0
14	TD	12.5	AXP	13.3	INTC	11.0	HYNMTR	11.6	RY	14.9
15	QPETRO	12.5	MUFG	13.2	TOYOTA	10.9	LLY	11.5	AVGO	14.0

Data as of December 2025. *Note: Includes $27.3bn of investment-grade data center project finance issued by Beignet Investor LLC and backed by Meta. Source: Goldman Sachs

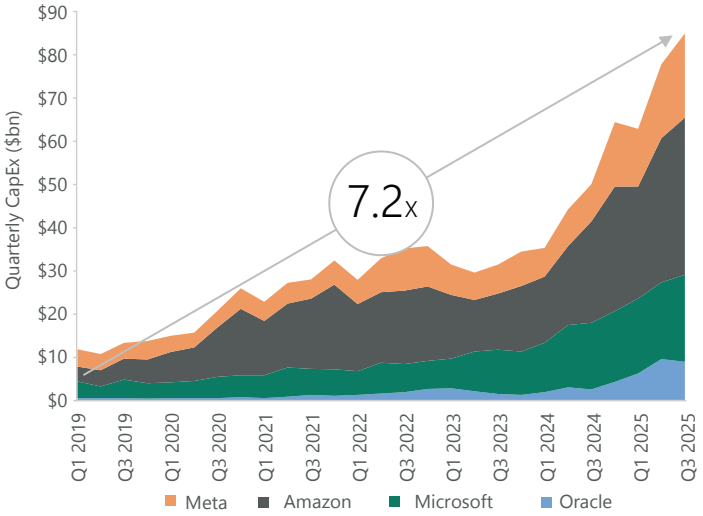
[7] JPMorgan, *AI capex - financing the investment cycle*, November 2025.

HYPERSCALERS PIVOT TO DEBT

Building the infrastructure required to train and run frontier models—compute, networking, power and data centers—demands investment on a scale typically associated with government-led industrial policy. For context, the Dwight D. Eisenhower National System of Interstate and Defense Highways launched in 1956 was built over nearly four decades, ultimately spanning roughly 50,000 miles and costing about $114 billion (roughly $634 billion in today's dollars).[8]

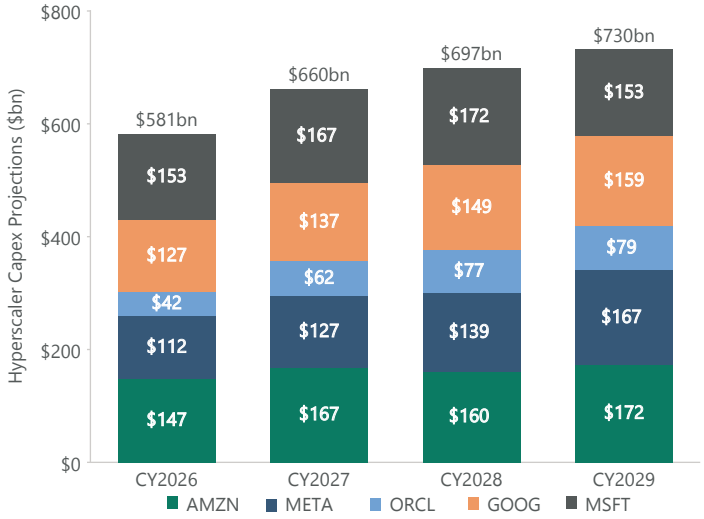
The estimated capex needs, especially if the more optimistic scenarios for AI adoption are realized, are staggering. Hyperscaler capex has already tripled since 2023, with Amazon, Meta, Oracle, Alphabet (Google) and Microsoft together sponsoring the largest private-sector infrastructure buildout in decades **(Exhibit 7)**. Sell-side forecasts now point to more than $2.7 trillion of cumulative outlays from 2025 to 2029, the majority tied directly to AI infrastructure **(Exhibit 8)**. Initial capex outlays were largely self-funded with internal cash flow, but we expect debt to play a more central role in funding the hyperscalers' capex programs going forward which will have meaningful implications for credit markets.

Exhibit 7: Hyperscalers' Capex Has Nearly Tripled Since 2023



Data as of November 2025. Sources: Pitchbook, Yahoo Finance.

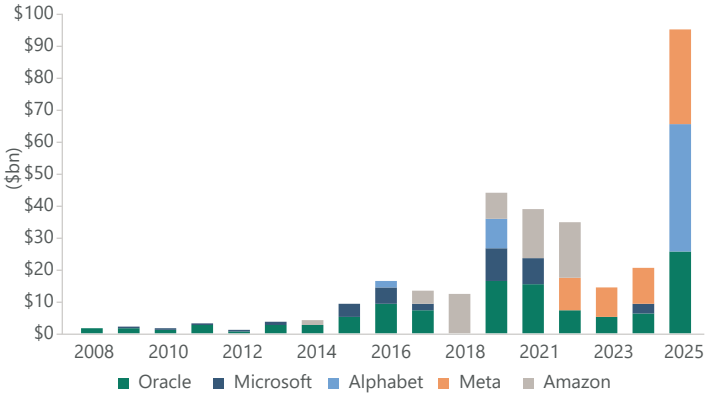
Exhibit 8: Hyperscalers Are Projected to Spend $2.7 Trillion Through 2029 on AI Infrastructure



Data as of September 2025. Source: S&P Capital IQ

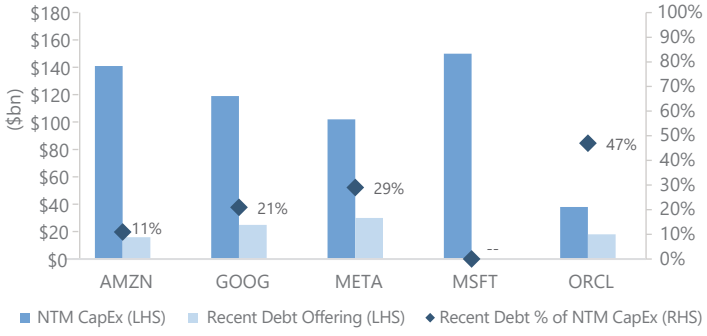
This pivot is already visible in recent debt issuance patterns. In the last three months of 2025, Oracle, Meta, Google and Amazon priced multibillion-dollar deals totaling $90 billion **(Exhibit 9)**. Oracle raised debt equivalent to nearly 40% of its $50 billion fiscal year 2026 capex guidance, while Meta and Alphabet issued debt equivalent to approximately 30% and 20% of their fiscal year 2026 capex forecasts, respectively. These debt issuances represent a material shift in these companies' historical reliance on cash flow-funded financing models **(Exhibit 10)**.

Exhibit 9: Hyperscaler Debt Issuance



Sources: Bloomberg. Debt issuance in US dollars from January 1, 2008 through November 6, 2025. Meta issuance excludes Beignet deal.

Exhibit 10: Recent Hyperscalers' Debt Offerings Vs. Capex

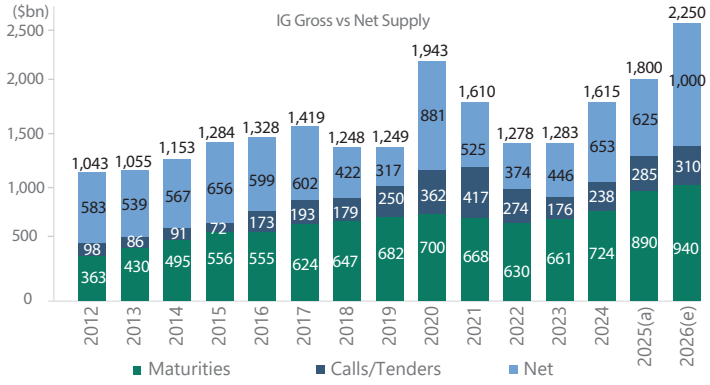


Source: Bloomberg. Next twelve months (NTM) Capex reflects consensus as of November 20, 2025.

[8] Federal Highway Administration.

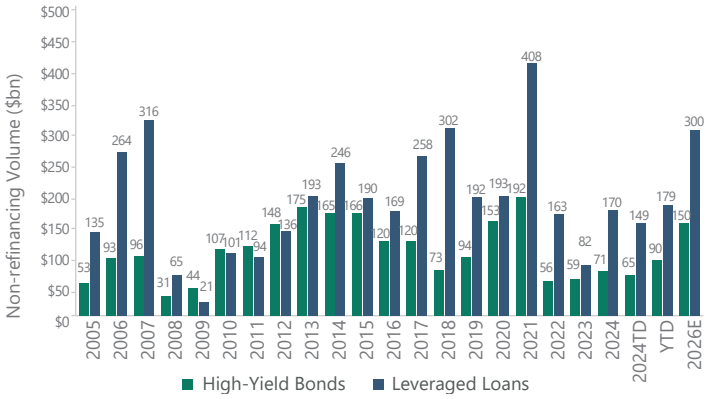
Sell-side expectations for 2026 show large increases in both IG and leveraged finance net supply. Morgan Stanley expects IG net supply to rise to new all-time highs of **$2.25 trillion** (gross) and **$1 trillion** (net) **(Exhibit 11)**. At the same time, HY and leveraged loan issuance is expected to reach roughly $450 billion next year, representing the highest combined volume since 2021 **(Exhibit 12)**.

Exhibit 11: Expected Public IG Issuance in 2026



Data as of December 2025. Source: Bloomberg, Dealogic, Pitchbook | LCD, Federal Reserve, Morgan Stanley Research forecasts

Exhibit 12: HY & LL Issuance



Data as of December 2025. Source: JPMorgan

Importantly, the hyperscaler debt issuance figures still understate the true scale of AI-related credit formation. They exclude large private credit financings that fund hyperscaler infrastructure but occur outside traditional public bond markets. A prominent example is Meta's Beignet structure, a special purpose vehicle used to finance the construction of dedicated data center capacity through asset-level, private-market debt backed by long-term lease commitments.[9] Oracle has pursued a similar approach, relying almost entirely on leased data center capacity financed through project-level structures rather than its own balance sheet.[10] In both cases, the capital ultimately supports hyperscaler AI capex, creates long-dated fixed obligations and absorbs substantial credit capacity—but remains invisible in public issuance statistics. This dynamic is precisely what we highlighted in last year's Credit Outlook: as the scale, asset life, and capital intensity of AI infrastructure approaches the limits of traditional bank and ABS markets, bespoke private IG financing becomes a necessary part of the solution.

RESHAPING THE INVESTMENT-GRADE UNIVERSE

For credit markets, that shift has two key implications. First, the hyperscalers will grow to become among the largest issuers in the IG market. Second, a deluge of high-quality issuance will push risk premia higher across the IG and high-quality BB-rated space.

1. The composition of the index is already tilting toward tech-led growth issuers. As **Exhibit 13** illustrates, funding just 20% of AI capex through IG markets would propel Amazon to the third-largest issuer in the public IG benchmarks by 2030, while Meta, Microsoft, Oracle, and Google would all move into the top 10—with Google rising from 67th to 8th. Further, hyperscaler issuance will likely be more skewed to longer duration issuances increasing their impact on index returns.

[9] Bloomberg, Meta, *Blue Owl Seal $30 Billion Private Capital Deal for AI*, October 2025.
[10] Apollo analysts, December 2025.

Exhibit 13: How AI-related Funding Will Reshape Credit Markets

Current Largest IG Issuers

Ticker	Rank	Weight
JPM	1	1.9%
BAC	2	1.7%
MS	3	1.6%
C	4	1.2%
WFC	5	1.2%
GS	6	1.2%
ORCL	**7**	**1.0%**
T	8	1.0%
HSBC	9	0.9%
VZ	10	0.9%
CMCSA	11	0.8%
AMZN	**15**	**0.7%**
META	**17**	**0.6%**
MSFT	**42**	**0.4%**
GOOGL	**67**	**0.3%**

As hyperscalers seek to fund capex through debt issuance, the composition of the investment grade market will evolve.

After Funding 20% AI Capex

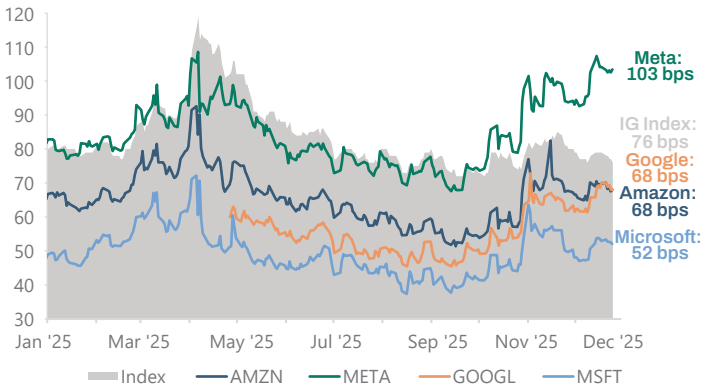
Ticker	Rank	Weight
JPM	1	1.8%
BAC	2	1.6%
AMZN	**3**	**1.6%**
MS	4	1.5%
META	**5**	**1.4%**
MSFT	**6**	**1.4%**
ORCL	**7**	**1.2%**
GOOGL	**8**	**1.2%**
C	9	1.2%
WFC	10	1.2%
GS	11	1.1%
T	12	0.9%
HSBC	13	0.9%
VZ	14	0.8%
CMCSA	15	0.8%

Data as of December 2025. Sources: Bloomberg, BofA. Assumes hyperscalers issue IG debt to fund 20% of BBG consensus Capex 2026-2029, while rest of IG index grows at 5% / year.

In addition to the large issuer sizes, this has implications for factor exposures. If the index is increasingly shaped by five companies pursuing similar strategic objectives, traditional sector labels become less useful. What looks like diversified exposure to online advertising cloud services, semiconductors, communications infrastructure and data-center REITs may in fact be one concentrated macro trade: long AI.

2. Not only will correlation risk increase, but the increased supply is likely to also push the market's "risk-free" spread anchor higher. As shown in **Exhibit 14**, long-dated hyperscaler bonds, despite being among the highest-rated issuers in the market, now consistently price close to or even wider than the significantly lower-rated IG index. For instance, AA-rated Meta debt trades wider than not only the IG Index (~80 basis points, A3/BAA1) but also BBBs (~100 basis points spread). This dynamic has the potential to reprice the entire market wider.

Exhibit 14: 30-Year Hyperscaler Spreads (AA+) Relative to the IG Index



Data from January 2, 2025 through December 26, 2025. Sources: Bloomberg, Federal Reserve US Economic Data (FRED).

RIPPLE EFFECTS: WHAT THIS MEANS FOR SOFTWARE CREDIT RISK

The unprecedented scale of AI investment now underway will ultimately need to translate into revenue and cash flow, a dynamic that has become a central focus for markets and a key driver of the AI-related volatility seen in recent months. We estimate that at least $1.5-$2 trillion[11] of annual AI application revenue will be needed by 2030 to support more than $5 trillion of expected data-center capex. While AI application revenue is growing rapidly, it remains far short of that level today, at roughly $40–$60 billion in 2025,[12] underscoring the magnitude of the monetization challenge embedded in the current investment cycle.

[11] Estimates are based on Apollo internal analysis and scenario-based demand projections for AI infrastructure and applications. Figures are intended to illustrate the scale of revenue required to support forecasted AI datacenter demand, not just existing projects.
[12] Apollo analysts.

Importantly, AI-driven revenue growth is unlikely to be purely additive. A meaningful portion will be zero-sum, potentially coming at the expense of some incumbent software providers through wallet-share shifts, pricing compression, and functional substitution. Profit pools are likely to migrate toward platforms with structural advantages in data and distribution, while software categories with overlapping or easily replicated functionality face heightened disruption risk. AI coding tools offer an early example: coding has emerged as the first scaled enterprise use case to deliver immediate, measurable returns, driving rapid adoption and generating an estimated $4 billion of annualized revenue today, with the majority captured by AI-native entrants such as Cursor, Anthropic, OpenAI and Cognition rather than traditional incumbents.[13] As these tools compress development cycles and automate large portions of the software lifecycle, they are reshaping software economics[14] and providing a template for how disruption—and credit risk—may propagate across the broader software market.

PORTFOLIO IMPLICATIONS: CONCENTRATION, CORRELATION AND THE NEED TO LOOK ELSEWHERE

From a portfolio standpoint, the AI financing boom has penetrated virtually every corner of the credit market. IG, AI-linked issuance has become a dominant driver of primary supply; in ABF, securitizations tied to data-center development have scaled rapidly; and in commercial real estate, lenders are increasingly financing land, power, and construction for hyperscale facilities pre-leased to AI-driven tenants such as Oracle. Beyond this, AI is also embedded in project finance, semiconductors, cloud software, and portions of leveraged credit, as hyperscalers increasingly partner with private capital to fund infrastructure off balance sheet.

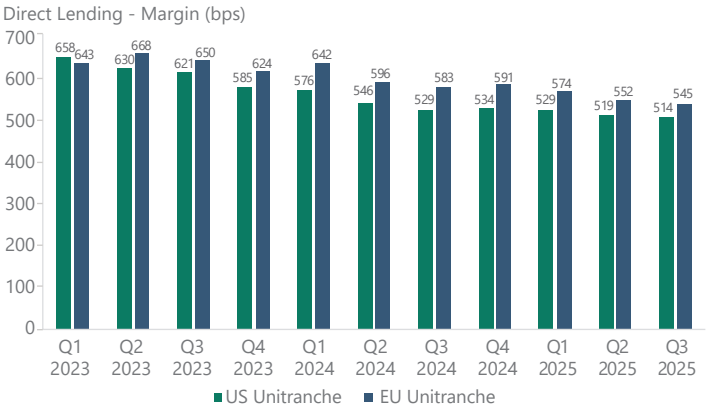
In other words, allocators may be taking on a growing, often hidden, "AI beta" across asset classes. Oracle's latest earnings call illustrated this dynamic clearly, as the company outlined a broad menu of financing avenues for its AI expansion—including chip-leasing from suppliers, customer-provided chips, and the flexibility to draw on public bond, bank and private debt markets—without committing to a single path.[15]

That makes diversification more valuable—*and more challenging to find*. Investors looking for uncorrelated exposure need to focus on parts of the market structurally insulated from the AI arms race. For fixed income investors, this means considering a broader set of assets. Two large opportunities stand out in particular:

- **European private credit.**

Although we expect some of the public hyperscaler issuance to eventually spill over into European markets, the region remains far less exposed to hyperscaler capex intensity, with issuance patterns likely driven more by traditional corporate refinancing and sponsor activity than by platform-scale AI investment. AI-linked issuance in Europe last year has been minimal, limited to Google's $13.25 billion euro-denominated bond sale.[16] This makes it a useful counterweight for portfolios with heavy IG or tech-tilted US exposure. In addition, slower bank disintermediation and constrained regional lenders have created a persistent supply–demand gap. This allows private credit managers to command wider spreads and tighter covenants than in the US, while regulatory conservatism and the lower penetration of direct lending make Europe a true credit-picker's market. Finally, regulatory fragmentation, multi-currency structuring, and legal complexity offer the opportunity for additional yield for global allocators **(Exhibit 15)**. You can read more on this in our white paper The Continental Shift: Europe's Private Credit Moment.

Exhibit 15: European Direct Lending Deals Tend to Price at a Premium



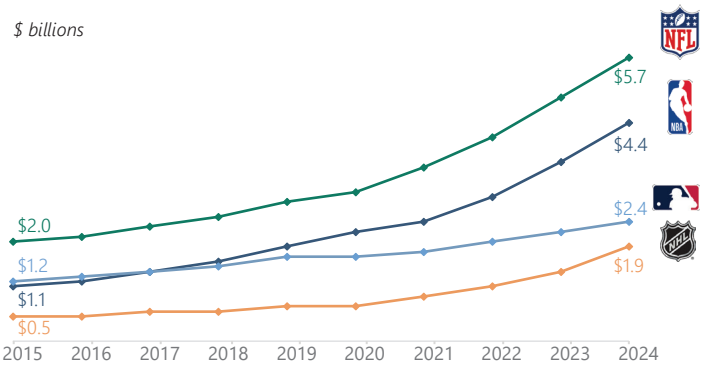
Data as of September 2025. Source: KBRA

[13] SemiAnalysis, October 2025.
[13] Claude software engineer lead, December 2025.
[14] Oracle, Fiscal Year 2026 Second Quarter Earnings Call, December 2025.

Sports financing.

Sports assets are uniquely insulated from AI-related disruption: their core product is elite human performance, a scarce and emotionally resonant experience that technology cannot replicate, automate or disintermediate. This durability is borne out in the data—franchise values have compounded at roughly 13% annually for more than 60 years, supported by fixed supply, global fan loyalty and the rising value of must-watch live content **(Exhibit 16)**. Against a backdrop in which AI is reshaping traditional industries and introducing new forms of correlation risk, we believe sports is one of the few sectors immune to the AI substitution curve. Demand for premium live events continues to rise, reinforced by community identity, unique in-person experiences and media ecosystems built around real-time engagement. These characteristics translate into low AI correlation, diversified recurring revenues, and strong long-term visibility, making sports a uniquely durable and scarcity-driven addition to a credit portfolio. You can read more on this in our recent white paper The Financing Gap in Sports: Unlocking a $2.5 Trillion Opportunity.

Exhibit 16: Average Team Valuation by League

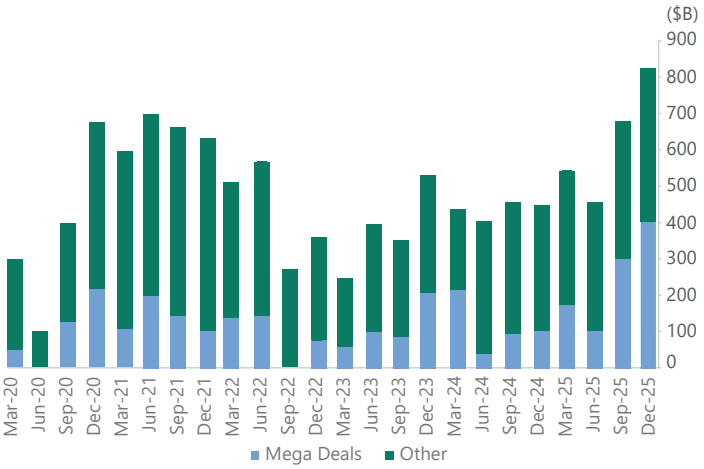


Sources: Forbes, From The Oilers To The Warriors: The Franchises That Scored Highest Jumps In Value Over The Past 20 Years, December 2021; Sports Business Global Media Report 2024; Deep Markets Insights Global Sports Sponsorship

Theme 2: The Return of the Megadeal

M&A momentum began to build in the summer of 2025 as easing financing conditions and improved confidence revived appetite for large, strategic transactions. The inflection point came in July, when Union Pacific agreed to acquire Norfolk Southern in a $72 billion cash-and-stock deal, creating the only US transcontinental railroad.[17] Momentum carried into early fall as private equity re-embraced super-sized transactions, highlighted by the announced $55 billion take-private of video game publisher Electronic Arts in September, the largest leveraged buyout on record. In November, the rebound broadened to strategic consumer M&A, with Kimberly-Clark's $48.7 billion cash-and-stock acquisition of Kenvue, the maker of Tylenol, Band-Aid and Listerine, combining iconic household and health brands into a global health and wellness leader. By December, competing bids for Warner Bros. Discovery—$104 billion from Paramount and $98 billion from Netflix—clearly signaled that the market had rediscovered its appetite for size. Funding for many of 2025's largest announced transactions will spill into 2026, providing an early signal of how capital structures may evolve to accommodate the return of the megadeal **(Exhibit 17)**.

Exhibit 17: US M&A Activity



Data as of December 2025. Source: Bloomberg

The resurgence in M&A activity in the second half of 2025 is not surprising and reflects the supportive environment for M&A that has emerged over the past 12 months. Lower financing costs, workable valuations across much of the corporate universe and more supportive government policy have converged into a powerful tailwind for M&A activity. Together, we expect these forces will further support dealmaking activity in 2026, expanding the universe of viable targets, increasing headline supply through acquisition-related financings, influencing relative credit performance and pushing issuers toward more innovative capital structures as deal sizes grow. As AI-driven capex is increasingly financed through the IG markets, a parallel wave of strategic and sponsor-led M&A transactions will contribute additional credit supply across both IG and HY.

[16] Goldman Sachs, December 2025.
[17] Bloomberg, December 2025.

DRIVERS OF THE SURGE IN M&A:

1. Falling cost of financing:

One of the catalysts for the resurgence in M&A is the continued decline in funding costs. Lower financing costs improve the economics for acquisitions, making larger and more complex deals economically viable. The shift in leveraged finance is particularly notable: leveraged loan yields have fallen from more than 10% in 2023 to below 8% today. With the market pricing in two interest rate cuts this year, loan yields will likely continue to drift lower, potentially approaching 7% in 2026 **(Exhibit 18)**. IG yields have also dropped during the same timeframe, though at a more modest pace, falling to below 5% from roughly 6%.

2. Reasonable valuations for much of the corporate universe

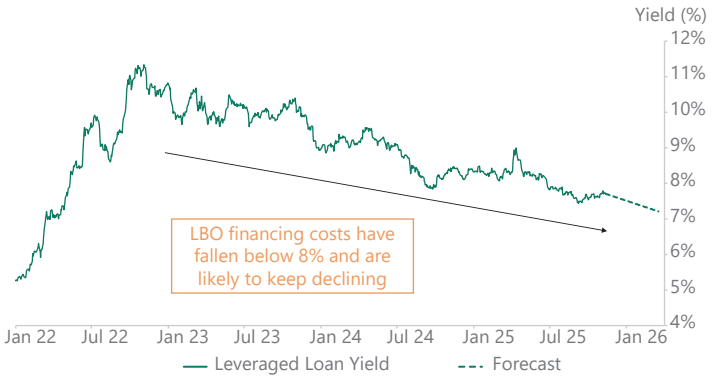
Reasonable valuations are also helping to support dealmaking activity. While headline S&P 500 P/E multiples appear elevated, they are skewed by the index's concentration: The Magnificent Seven (Mag 7) account for roughly one-third of the S&P 500's weight (34%) and trade at an average PE multiple of about 40x. Still, the equal-weighted S&P trades near 18 times earnings, a level that looks far more attractive once paired with a declining cost of capital **(Exhibit 19)**.

Meanwhile, sponsors are sitting on a large amount of dry powder. While this is not a new phenomenon, falling lending costs increase the likelihood that this stockpile of investable capital is put to work, creating an additional source of demand that could meaningfully support a pickup in M&A activity **(Exhibit 20)**.

3. Policy Tailwinds

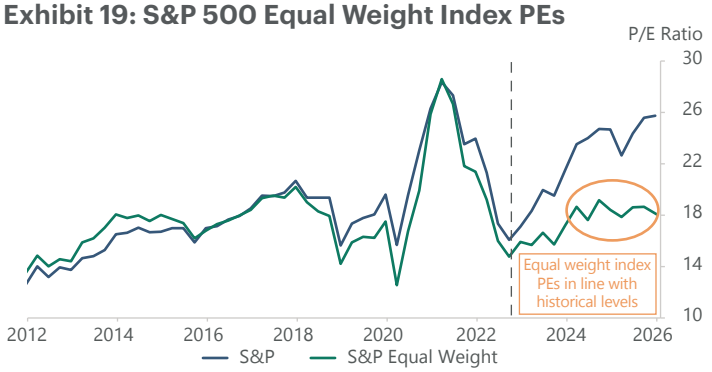
For much of the past three years, M&A volumes sat well below historical averages. Expectations were that activity would reaccelerate early in 2025 as the new administration took office. And while the Trump administration has been broadly supportive of capital markets through its lighter regulatory touch and pro-business policies, the tariff volatility that dominated the first half of the year forced many companies to pause strategic decisions. As tariff concerns subsided and the Fed began cutting rates, the opportunity set in M&A came into clearer view. Further, the relaxation of antitrust enforcement has unlocked transactions that would have struggled to clear regulatory review in prior years, including the proposed WBD/Netflix combination, Fifth Third Bancorp's acquisition of Comerica and a revised partnership between US Steel and Nippon Steel.

Exhibit 18: Leveraged Loan Yields Drifting Lower



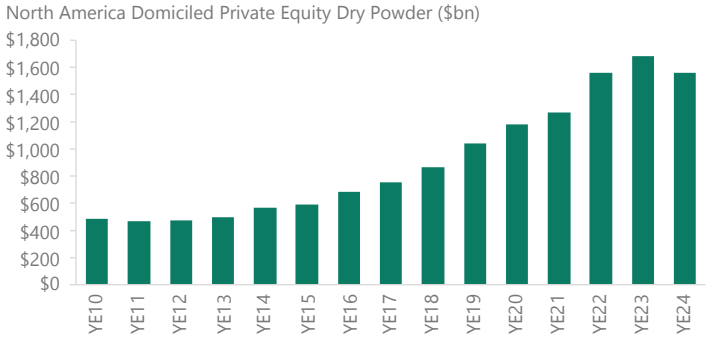
Data as of November 2025.
Source: JPMorgan Leveraged Loan Index

Exhibit 19: S&P 500 Equal Weight Index PEs



Data as of November 2025. Source: Bloomberg

Exhibit 20: Private Equity Dry Powder



Data from 2010-2024. Sources: Preqin, Barclays Research

At the same time, the $3.4 trillion One Big Beautiful Bill Act (OBBBA) adds an important policy tailwind for dealmaking, with corporate provisions that restore full and immediate expensing for capital investment and domestic R&D and expand interest deductibility.[18] By lowering after-tax financing costs and improving post-deal cash flow, the legislation further enhances the economics of capex and debt-financed M&A.

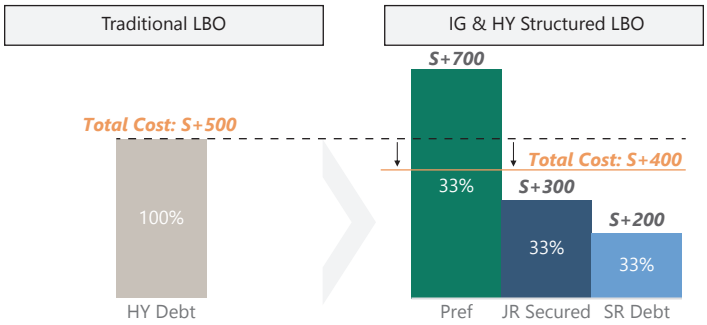
[18] Bipartisanpolicy.org, *What Does the One Big Beautiful Bill Cost,* July 2025

A notable trend in recent M&A activity is the extent to which the government has inserted itself in corporate dealmaking among strategically important sectors. The government is now playing a far more consequential role in steering the direction of M&A than at any point in the past decade. This includes the US government's $9 billion equity investment in Intel—amounting to roughly a 10% stake—and the Department of Defense's $400 million equity stake in MP Materials.[19] Another example is EchoStar, where recent FCC actions reduced regulatory uncertainty around spectrum transfers and contributed to the company's decision to monetize the bulk of its wireless spectrum through sales to incumbent carriers.[20]

AN LBO-ABLE MARKET

With 2025 delivering the largest roster of megadeals in recent history,[21] the momentum behind a meaningful upswing in LBO volumes is building. Against this backdrop, issuers are turning to more creative funding solutions. To support record-scale deals, borrowers are increasingly using multi-tranche structures that tap several pockets of the credit markets at once—an evolution made necessary as single-tranche HY unitranches become difficult for investors to absorb once deal sizes exceed $10 billion. In a stylized example shown in **Exhibit 21**, these structures can lower all-in financing costs by roughly 100 basis points for the largest issuers, widening the universe of companies that are realistic acquisition targets for private equity buyers.

Exhibit 21: LBO Funding Solutions



Source: Apollo Analysts

Taken together, we believe these dynamics point to a market that is structurally better positioned to absorb large, complex transactions. As financing flexibility improves and interest rates moderate alongside a favorable antitrust regulatory environment, conditions are aligning for a secular upswing in M&A. For credit markets, the return of large-scale M&A and its related financing needs reinforces the view that a buyer's market in credit is developing.

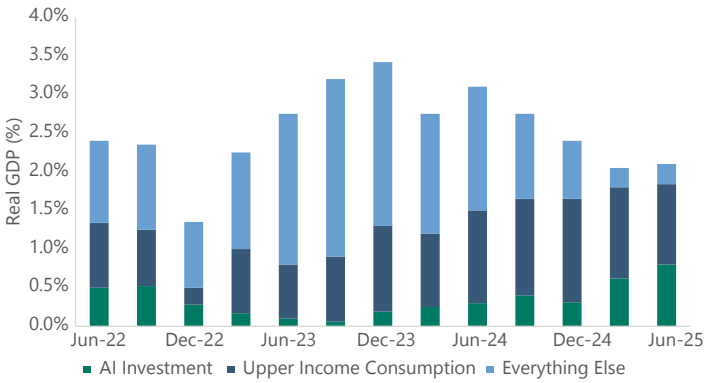
Theme 3: K-Shaped Credit

As the economic cycle enters its next phase, the defining feature of the macro backdrop is not weak growth, but increasingly narrow growth. As we mentioned earlier in the outlook, headline indicators across the US economy remain resilient, yet that strength is becoming more unevenly distributed. Economic gains are concentrated among higher-income consumers and large, AI-exposed corporates, while pressure is building across more rate- and income-sensitive households and businesses.

This K-shaped divergence is now evident in day-to-day consumption behavior and corporate investment decisions and is beginning to shape credit fundamentals. Importantly, this does not signal broad-based consumer weakness. Instead, it reflects a shift toward credit dispersion, as capital access and balance-sheet strength diverge beneath resilient headline data—mandating greater investor selectivity.

AI has accelerated this bifurcation. Capital spending growth over the past year has been heavily concentrated in AI-related infrastructure, benefiting large, well-capitalized firms and asset owners **(Exhibit 22)**, while expectations for AI-driven productivity gains are reshaping corporate hiring—particularly at the entry level.[22] At the same time, rising asset prices continue to support spending within higher income brackets, masking growing stress beneath the surface.

Exhibit 22: AI Investment and High-Income Spending Supporting Growth



Data as of June 2025. Source: BEA, Haver, UBS (assuming upper income accounts for 40-60% of consumption)

[19] TechRepublic, August 2025.
[20] ViaSatellite, May 2025.
[21] Bloomberg, December 2025.
[22] Stanford Social Innovation Review, *A new AI Career Ladder*, October 2025.

CONSUMER

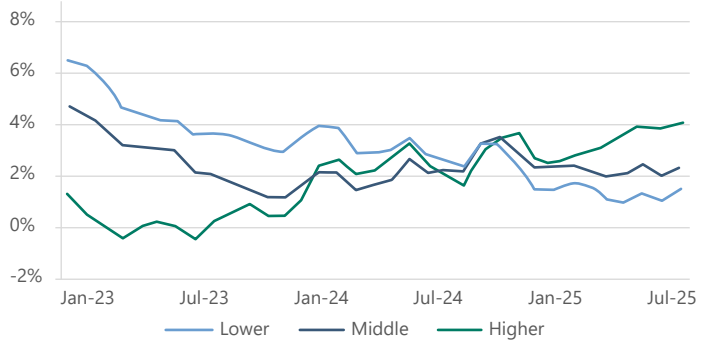
While aggregate income and spending have remained resilient, the underlying trajectory has diverged meaningfully across income cohorts. Recent data show that real wage growth for lower-income households has continued to decelerate, falling to roughly 1.4% year-over-year in November, compared with approximately 4.0% growth for higher-income households **(Exhibit 23)**. This gap marks a reversal from the early post-pandemic period and implies outright pressure on incomes for lower-income consumers, adjusting for inflation.

This income divergence is translating directly into consumption behavior. Spending growth for lower-income households slowed to 0.6% year-over-year in November, materially lagging the 2.6% pace observed among higher-income consumers **(Exhibit 24)**. In contrast to earlier phases of the cycle—when spending patterns across income cohorts moved largely in parallel—recent data show a sustained and widening gap. Elevated asset prices have helped insulate higher-income households, where financial asset ownership is concentrated, allowing spending to reaccelerate even as wage growth moderates. Lower-income households, with limited exposure to asset appreciation and more vulnerability to rising prices and slower income growth, are increasingly constrained, reinforcing a K-shaped consumption dynamic that has become more pronounced over time.

Recent earnings commentary highlights how sharply consumption is diverging across income cohorts. Chipotle Mexican Grill reported a broad-based pullback in dining frequency last year, followed by a widening gap in which lower- and middle-income consumers continued to reduce spending, particularly among younger households. Walmart echoed a similar pattern, noting moderating spending among lower-income shoppers while middle- and higher-income customer purchasing trends remained, with higher-income cohorts increasing spend in certain categories. Meanwhile, Delta Air Lines has emphasized growing strength at the top end of the market, with premium travel demand accelerating and premium cabin revenue on track to overtake coach sales, underscoring the strength in discretionary spending by higher-income consumers.[23]

Exhibit 23: Wage Growth Across Incomes

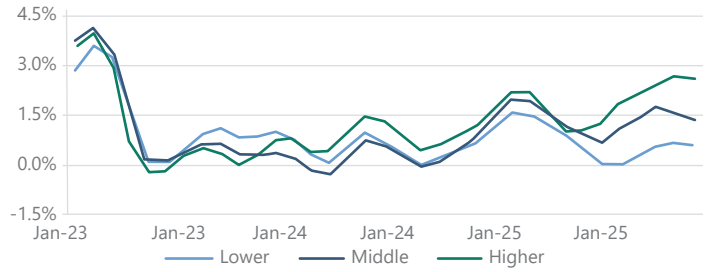
After-tax wage and salary growth by household income terciles, based on Bank of America aggregated consumer deposit data (3-month moving average, YoY%, SA)



Data as of Q3 2025. Sources: Morgan Stanley, Bloomberg, S&P Capital IQ

Exhibit 24: Spending Growth Across Incomes

Total credit and debit card spending per household, according to Bank of America card data, by household income terciles (3-month moving average, YoY%, SA)



Data as of Q3 2025. Sources: Morgan Stanley, Bloomberg, S&P Capital IQ

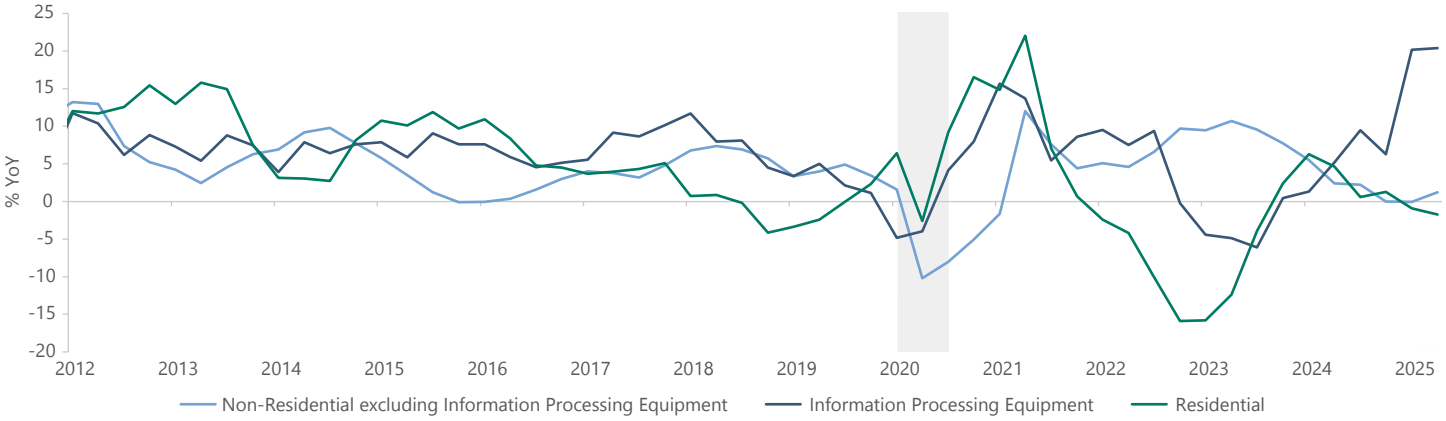
CORPORATES

A similar K-shaped dynamic is emerging across the corporate landscape. While aggregate corporate fundamentals remain solid, the headline strength obscures growing divergence beneath the surface. Capital spending, profitability and earnings expectations are increasingly concentrated among a narrow group of large, AI-exposed firms, while much of the broader corporate sector is enjoying limited investment momentum and more muted earnings growth.

[23] Bloomberg, Earnings call analysis, through December 2025.

Recent data show that nearly all of the growth in private fixed investment has been driven by information processing equipment, reflecting the race to build out AI-related infrastructure and compute capacity **(Exhibit 25)**. Outside of this category, non-residential investment has been broadly flat year-over-year, indicating little incremental capex across the rest of the economy. In other words, corporate investment has not accelerated broadly—it has been reallocated, with AI absorbing a disproportionate share of incremental capital while other sectors remain cautious.

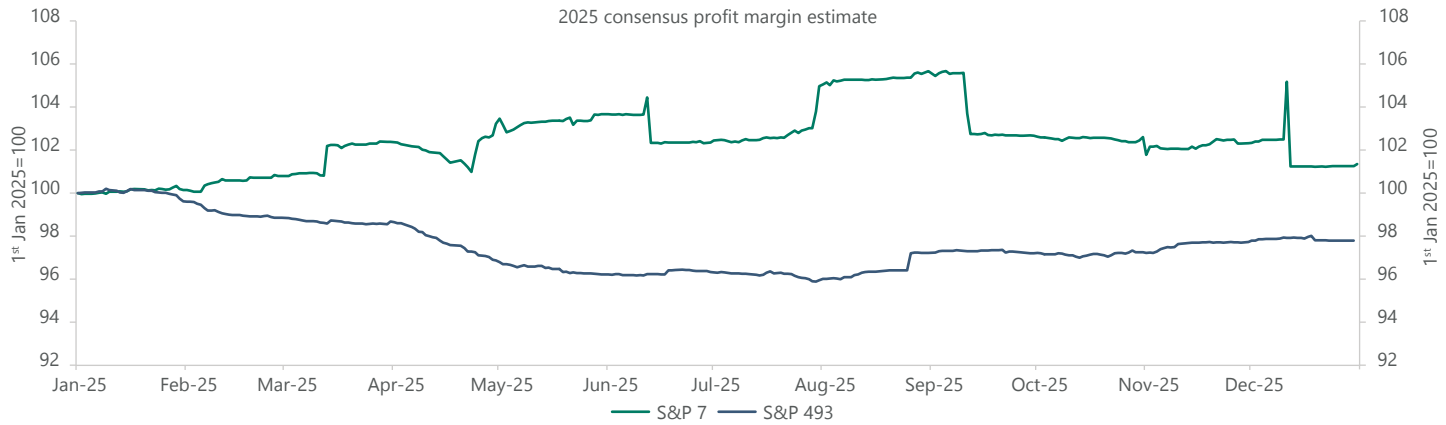
Exhibit 25: No Growth in Corporate Capex Outside of AI



Data as of Q2 2025. Sources: US Bureau of Economic Analysis (BEA), Macrobond, Apollo Chief Economist

This surge in tech investment has been underpinned by rising expectations for profit margins and earnings at the largest companies. Consensus estimates for the Mag 7 profit margins rose over the course of last year, while margins for the remaining S&P 493 companies have trended lower **(Exhibit 26)**. The result is a widening profitability gap, as margin pressure persists across more labor- and rate-sensitive businesses.

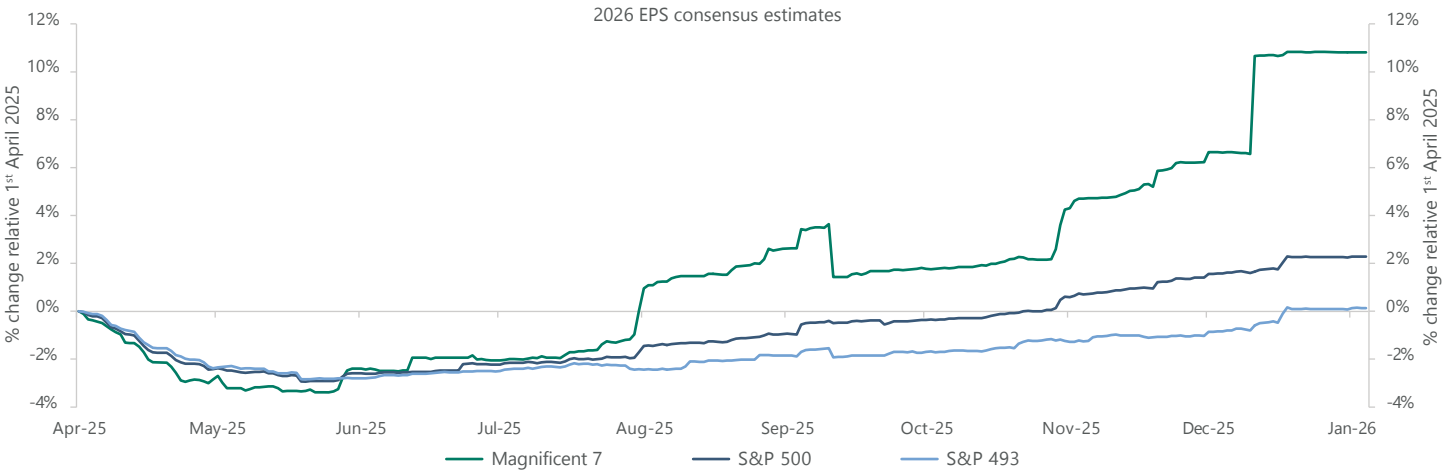
Exhibit 26: Profit Margins Rising for Mag 7 & Declining for the S&P 493



Data as of December 2025.
Sources: Bloomberg, Apollo Chief Economist.

Earnings expectations reinforce this pattern. After a brief pullback in April, 2026 earnings estimates for the Mag 7 were up roughly 6% last year, while earnings expectations for the rest of the index remained below their levels at the start of the year **(Exhibit 27)**. The gap has widened steadily through the year, underscoring how growth optimism is increasingly concentrated in AI beneficiaries rather than broadly distributed across corporate America.

Exhibit 27: Earnings Expectations Revised Up for Mag 7 & Down for the S&P 493



Data as of January 2026. Sources: Bloomberg, Apollo Chief Economist

Equity market performance reflects these same dynamics. Stocks most closely associated with AI-driven growth have materially outperformed, with the Mag 7 equities up 25%, compared with gains of 16% for the S&P 493.

Taken together, these trends point to a corporate sector that looks healthy in aggregate but is becoming increasingly bifurcated in practice. For credit markets, this matters because capital access, cash-flow durability and balance-sheet resilience are now far more dependent on a company's position within the AI investment ecosystem than on broad economic conditions alone.

Dispersion Over Distress

Despite pockets of softness in wages and employment, aggregate consumer credit performance has remained resilient. Stress remains concentrated among lower-rated borrowers, where it is both expected at this stage of the cycle and increasingly reflected in valuations. Importantly, vintages have shown signs of stabilization, supported by tighter underwriting standards, lower household leverage, and structurally improved balance sheets, particularly in residential credit, where loan-to-value ratios remain conservative. Absent a material deterioration in economic conditions, we do not see a compelling case for a broad-based weakening in consumer credit fundamentals.

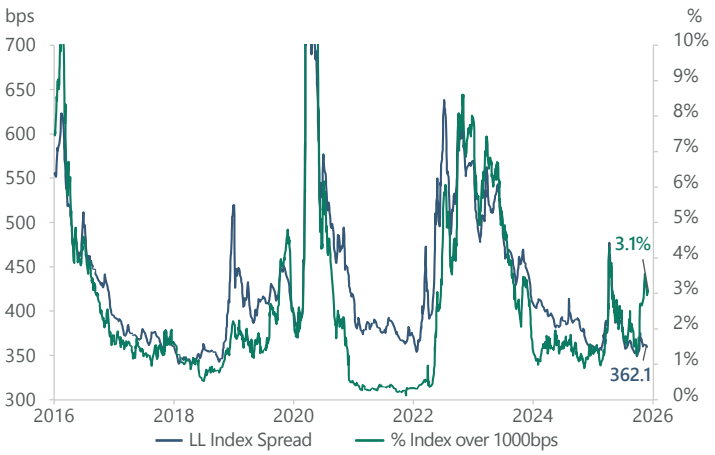
Recent headlines—specifically those surrounding Tricolor and First Brands—have focused on a small number of high-profile problem credits and have often been extrapolated as evidence of broader fragility. In our view, these cases are idiosyncratic. Events at Tricolor and First Brands reflect issues of governance, execution, and underwriting rather than a systemic deterioration in household credit quality. Markets have largely reached the same conclusion: securitized consumer credit spreads briefly widened in the immediate aftermath of these headlines but have since retraced, with ABS markets recovering as underlying performance data reaffirmed stability.

On the corporate front, default activity across leveraged credit declined meaningfully in 2025, with total defaults and liability management exercises totaling $67.8 billion—down 19% year over year and well below 2023 levels—as an approximately 40% reduction in distressed exchanges more than offset a roughly 30% increase in payment defaults.

However, similar to consumer trends, dispersion has become increasingly pronounced at the lower end of the quality spectrum. Volatility tied to tariffs and AI-related disruption has put additional pressure on already weaker borrowers. In 2025, aggregate high yield spreads were essentially unchanged, yet CCC spreads widened materially, rising roughly 85 basis points from 550 basis points to 635 basis points **(Exhibit 28)**. A similar dynamic has emerged in BB/B leveraged loans, where the share of the index trading above 1,000 basis points has increased to around 3%, even as aggregate spreads remain near historical tights, supported by resilient headline growth, solid fundamentals, and favorable technicals **(Exhibit 29)**.

Exhibit 28: HY Index vs CCC Index

Exhibit 29: BB/B Loan Index vs. % of Index over 1,000 bps



Data as of December 2025. Source: Bloomberg

This dispersion is not limited to valuations alone. Fundamental performance within corporate credit has also been increasingly bifurcated by rating. Over the past year, lower-quality CCC issuers have seen their leverage and interest coverage metrics deteriorate, while higher-quality single-B and BB borrowers have generally moved in the opposite direction, benefiting from steadier cash flows and improved balance-sheet discipline **(Exhibits 30, 31)**.

Exhibit 30: Leverage Worsened in CCCs, While Improving in BBs/Bs

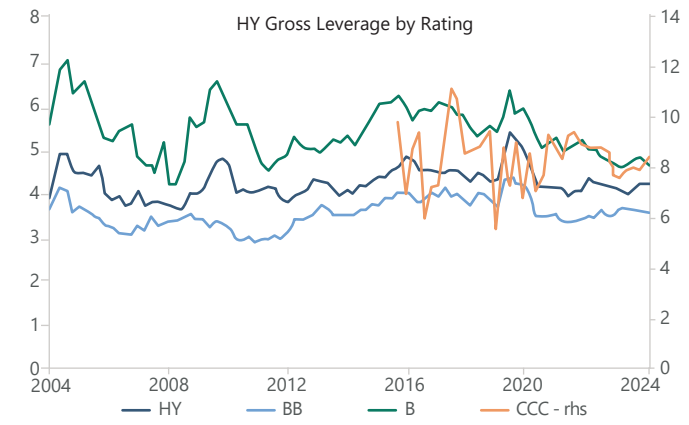
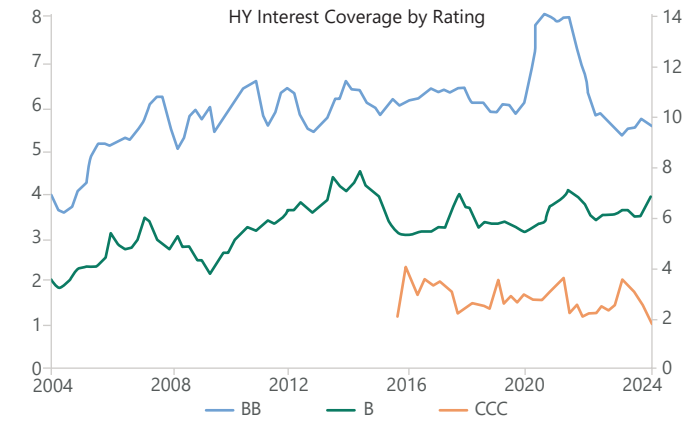


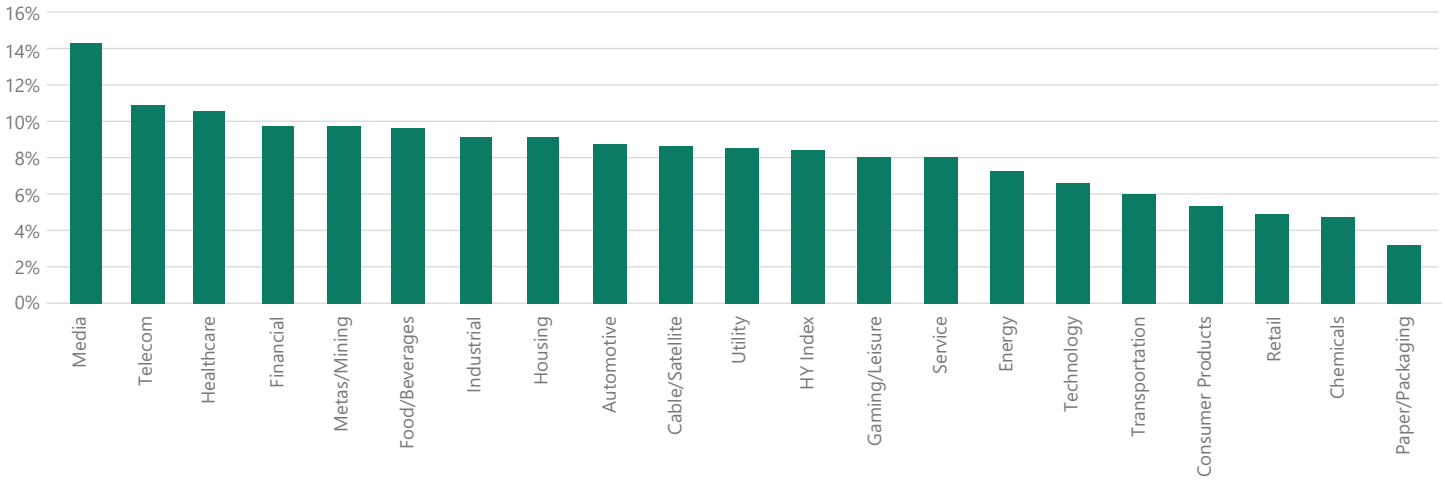
Exhibit 31: EBITDA Coverage Improved in Bs but Worsened Meaningfully in CCCs



Data as of September 2025. Source: Morgan Stanley

Dispersion was also pronounced across sector performance in the HY Index. While the index was up roughly 8% through mid-December, returns varied widely as investors became more selective. Media led the market, gaining more than 14% amid elevated M&A activity, while more cyclical and tariff-exposed sectors such as chemicals and packaging lagged, posting gains of less than 5% **(Exhibit 32)**.

Exhibit 32: 2025 High Yield Bond Performance Across Sectors



Data as of December 2025. Source: JPMorgan

Ultimately, this dispersion—across consumer, corporates and issuers—is another clear signal that credit markets have shifted back into a buyer's market. When growth is broad and liquidity is abundant, capital tends to be priced indiscriminately. When growth narrows, as it has across consumers, corporates, and capital spending, pricing power shifts back to lenders. In a K-shaped economy, borrowers are no longer competing on equal footing. Capital is becoming more discriminating, weaker balance sheets are being penalized, and stronger credits are increasingly willing to pay for certainty of execution. For buyers of credit, dispersion is not a warning sign, it is the mechanism through which attractive entry points emerge. This is not a market defined by forced selling or systemic stress, but by choice. And in credit, markets defined by choice tend to favor buyers.

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