BANKERS EDGE
ADVISORY

Credit Market Update

MAY 2026

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Executive Summary

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Growth is holding up, but its composition has shifted. Q4 2025 real GDP came in soft at 0.5%, carried by the consumer while government spending pulled back, before **Q1 2026 firmed to 1.6%**. The Atlanta Fed's GDPNow already points to a stronger **Q2 near 3.3%**, suggesting the late-2025 slowdown was a pause rather than a turn. The clearest downside risk remains energy – persistently high oil prices feeding into input costs, squeezing margins and eroding household purchasing power. The open question is whether that pressure stays cyclical or hardens into a structural headwind.

2

Corporate balance sheets are still in good shape. **Delinquencies held at 1.3% in Q1 2026** – comfortably below anything that would signal real credit stress. Capital markets remain open, lenders are selective but active, and private credit keeps filling the gaps left by more cautious banks. The backdrop for getting deals done remains intact.

3

Dealmakers aren't waiting for the dust to settle. **Global M&A topped $1.2 trillion in Q1 2026, up 26% year-over-year** as megadeals returned. Sponsors and strategic acquirers are putting capital to work through the uncertainty rather than waiting it out. The money and the conviction are both there – from here, the edge goes to whoever stays disciplined enough not to overpay.

US GDP Breakdown

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Q1 2026: Growth Regains Its Footing, Led by Capital Spending

US real GDP grew 1.6% in Q1 2026, a clear step up from a soft close to 2025 and well clear of recession territory. The standout was business investment, as spending on AI equipment and data-center construction accelerated. Even with elevated geopolitical uncertainty and an oil-price shock in the background, the mix points to an economy now leaning on capital formation rather than the consumer to push output higher.

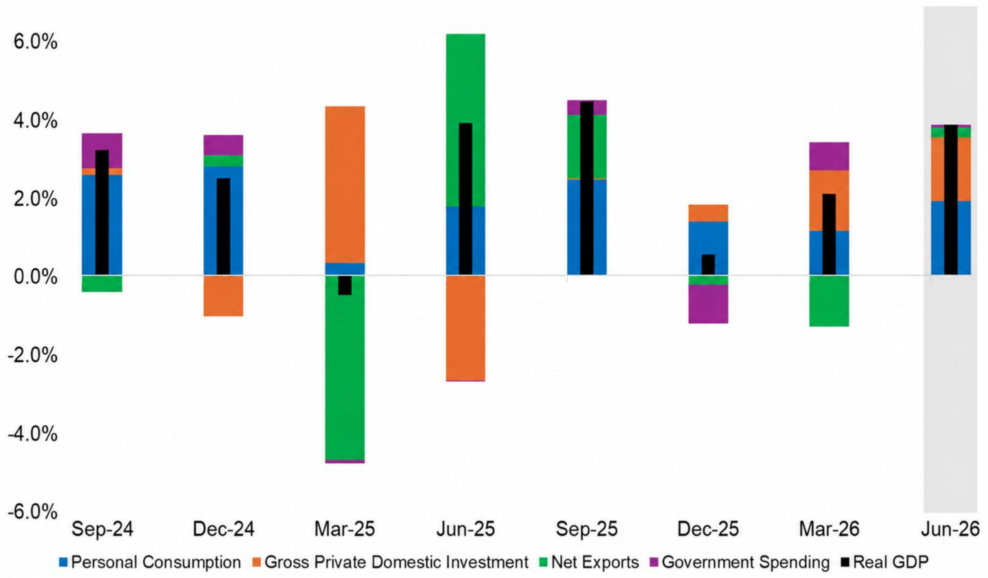
Private Domestic Investment: The AI-Driven Capex Cycle

In Q1 2026, investment wasn't just a contributor to growth, it was the engine. The build-out of AI infrastructure, from data centers to the equipment that fills them, did most of the work and shows little sign of cooling. Hyperscaler commitments are tracking toward roughly $440 billion of AI-specific spending this year, and the broader capex cycle is projected to add around 2.5 points to GDP in 2026 and over 3 points in 2027.

Q2 2026 GDP Nowcast: Momentum Building

The forward picture is firmer. The Atlanta Fed's GDPNow model has Q2 2026 tracking near 3.3%, building on Q1's 1.6% rebound, with steadier consumption, a renewed pickup in investment, and a smaller trade drag doing the work. If the nowcast holds, Q2 would be the strongest quarter since Q3 2025 and would put the late-2025 soft patch firmly in the rear-view mirror.

Contributions to Percent Change in Real Gross Domestic Product



Shaded area denotes forecasts, Atlanta Fed GDPNow

Source: Atlanta Fed GDPNow, June 10th 2026.

US Productivity

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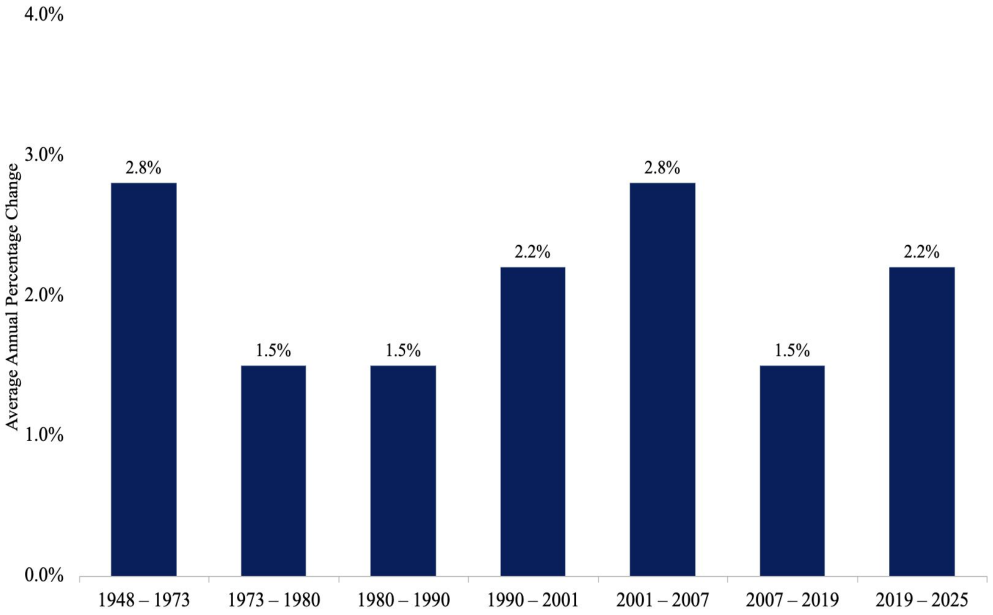
Productivity: Above Trend and Accelerating

Worker productivity continues to run ahead of its longer-run trend. Nonfarm labor productivity rose 2.2% in 2025 on an annual-average basis, and year-over-year growth was still a solid 2.8% in Q1 2026, even as the quarterly pace eased. The 2.0% annualized rate since Q4 2019 sits well above the 1.5% recorded across the 2007-2019 expansion, the economy continues to produce more output per hour worked than it did throughout much of the last decade. With AI adoption and capital-investment incentives reinforcing one another, there's little sign this run is finished.

The Bigger Story: A Structural Tailwind Is Building

The more compelling story is what comes next. Today's 2.0% trend is a respectable base, but the AI build-out is laying the physical and software infrastructure for a more durable, broad-based lift in enterprise productivity as these tools scale across industries. Policy is pushing the same way: the One Big Beautiful Bill Act permanently restored 100% bonus depreciation, lifted the Section 179 expensing cap to $2.5 million, and brought back immediate expensing of R&D - a tax code deliberately tilted toward the capital and equipment spending that expands productive capacity. The setup for a multi-year productivity step-up is arguably the strongest in a generation.

Productivity Change in Nonfarm Business Sector (1947-2025)



JOLTS Employment Survey Data

JOLTS: Openings Surge, but Churn Stays Low

The April 2026 JOLTS report shows job openings jumping 731,000 to 7.6 million, a near two-year high that lifted the openings rate to 4.6%. Total separations eased to 5.0 million and layoffs stayed contained at 1.7 million. The surge in postings was concentrated in professional and business services, leaving a picture of firm labor demand paired with still-low turnover.

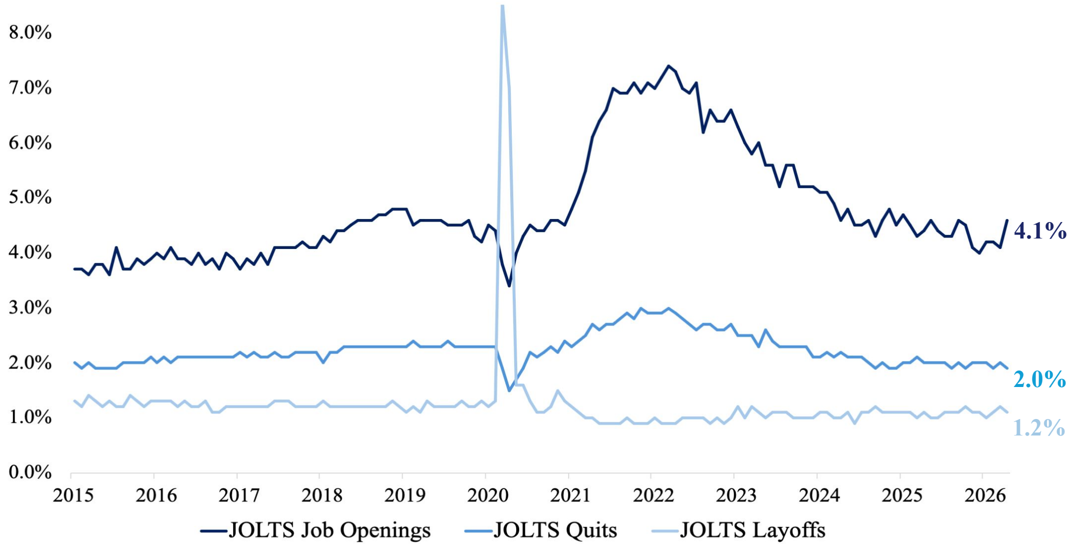
Hiring Eases as the Openings-Hires Gap Widens

After a strong March, hiring cooled in April: total hires fell 419,000 to 5.1 million, widening the gap between posted openings (7.6 million) and actual hires to roughly 2.5 million. The quits rate ticked down to 1.9%, extending the 'great stay' dynamic workers are staying put rather than chasing new roles. With openings rising while hiring slows, the data points to a 'low-hire, low-fire' market: demand is there on paper, but employers are filling roles slowly and deliberately.

Bottom Line: Stead, With Improving Momentum

The labor market is not falling apart, and the latest data suggests it may be re-accelerating. Layoffs remain contained, hiring is recovering from its February trough, and the gap between posted openings and actual hires is narrowing. This is a labor market to monitor, not one flashing warning signs.

JOLTS Job Openings, Nonfarm Quits, and Nonfarm Layoff Rates



Source: US Department of Labor Data, June 10th 2026.

Unemployment & Wage Growth

Employment: Strengthening, Not Just Steady

Unemployment held at 4.3% through Q1 and into May, but hiring picked up: nonfarm payrolls rose 172,000 in May, well above the ~80,000 consensus. The anticipated wave of AI-driven layoffs has yet to materialize; outside of pockets like financial activities, employers continue to add and retain workers despite economic uncertainty.

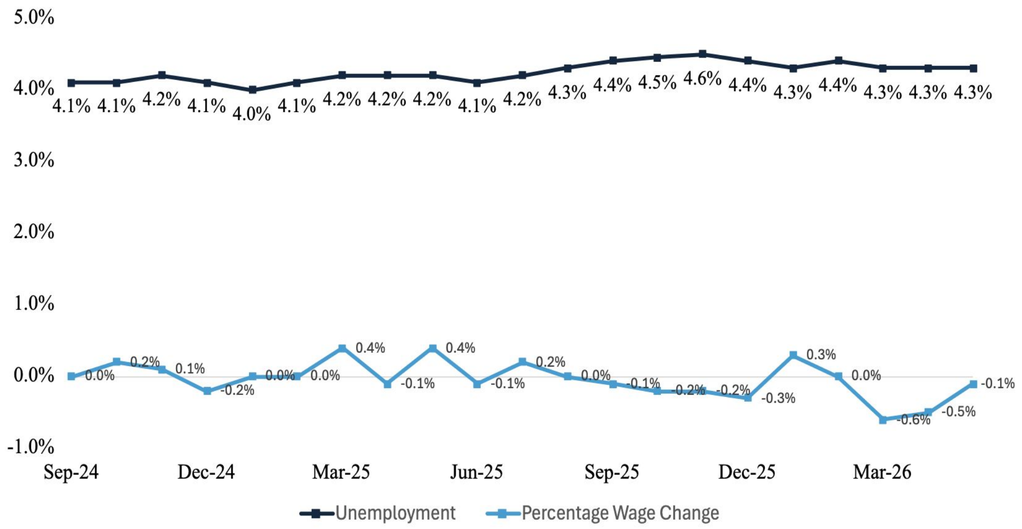
Wages: Real Pay Now Slipping

Real (inflation-adjusted) average hourly earnings have now slipped for consecutive months, 0.5% in April and 0.1% in May as price increases outrun nominal wage gains. Paychecks are still growing in dollar terms, but with tariffs and higher energy costs lifting the cost of living faster, workers' real purchasing power is quietly eroding. It isn't a wage collapse, but it is a clear break from the real-income growth that supported consumer spending through much of last year.

The Takeaway: A Tougher Trade-off for the Fed

The labor market itself is not the Fed's problem: hiring is steady, unemployment is low, and falling real wages actually argue against any wage-price spiral. The harder part is inflation. Price pressures are now strong enough to push real incomes negative even while employment grows which leaves policymakers with less room than a clean 'soft landing' would imply. A resilient jobs market buys patience, but it's inflation, not employment, that will dictate the next move.

US Unemployment Rate and Wage Growth Rate



Source: U.S. Department of Labor Data, June 10th 2026.

Consumer Financial Health

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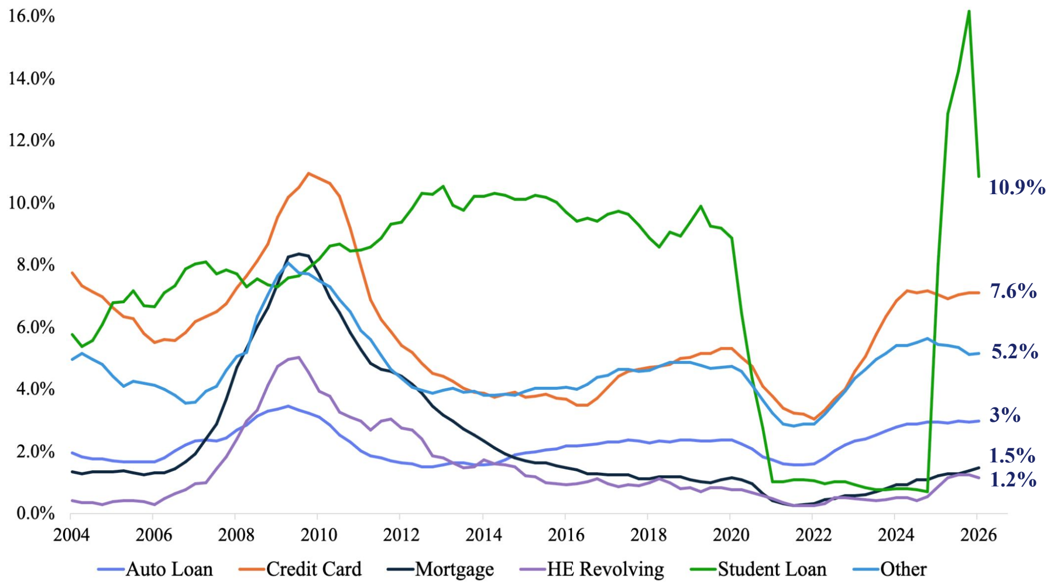
Consumer Credit: Manageable and Moderating

Overall consumer delinquency was steady at 4.8% of outstanding debt in Q1 2026. Credit card early delinquencies eased to 8.6% from 8.7%, a sixth straight quarter of improvement, while auto loan stress is decelerating, with early delinquency flows slipping to 7.7% from 8.0% a year ago. The strain stays concentrated among younger and lower-income borrowers, but household credit overall is holding well short of broad-based distress.

Student Loans: The Outlier Worth Watching

New student loan delinquencies cooled in Q1 2026, with the transition rate into serious delinquency falling from 16.2% to 10.9% as the first post-forbearance default wave clears the system. Even so, the stock of seriously delinquent balances kept climbing to 10.3%, and 2.6 million borrowers defaulted in the quarter alone. This is stabilization, not genuine recovery. Impaired credit among younger borrowers risks delaying homeownership, curbing discretionary spending, and weighing on industries levered to younger consumers.

Transition into Serious Delinquency by Loan Type (90+)



Source: Federal Reserve New York, Q1 2026.

Corporate Financial Growth

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Margins: Profitability Strong, but Cost Pressure Reappearing

S&P 500 net profit margins remained strong in Q1 2026, reaching 14.7%, up from 13.2% the prior quarter and above the five-year average. However, the gross margin data now shows a sharper reset, falling to 63.4% after holding near 70% through late 2025. The takeaway is still constructive, but more balanced: companies are protecting bottom-line profitability, while higher input costs are beginning to show up at the gross margin level.

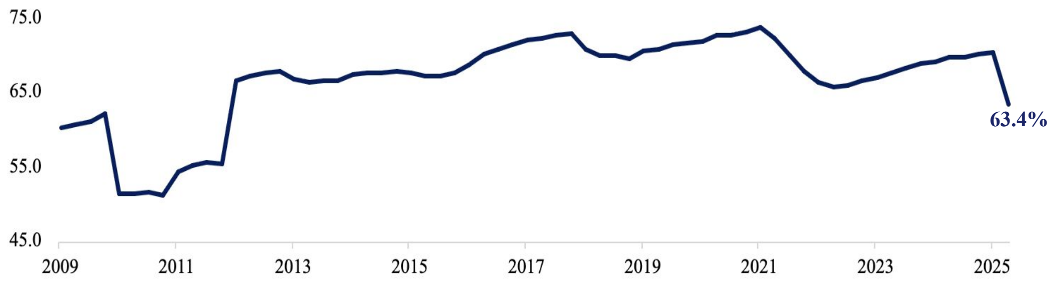
Credit: Low Delinquencies, but No Longer Falling

Corporate credit conditions remain healthy, though the data is no longer improving. Business loan delinquencies were 1.34% in Q1 2026, essentially unchanged from Q4 2025 and still well below prior cycle stress levels. That suggests balance sheets remain broadly solid, but the gradual move higher from 2024 levels shows that tighter financing conditions and slower growth are starting to work through the system.

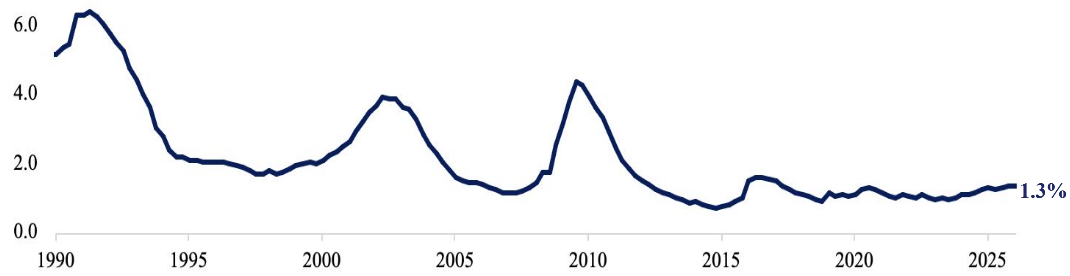
Capital Markets: Open and Active

The deal-making backdrop is firmly intact. Global M&A topped $1.2 trillion in Q1 2026, up 26% year-over-year, as sponsors and strategic acquirers kept deploying capital through the uncertainty. Funding remains readily available, and the mix of solid fundamentals, contained credit stress, and active private credit markets continues to support transaction activity.

S&P 500 Gross Margins (%) Since 2010



Delinquency Rate on Business Loans, All Commercial Banks



Sources: Federal Reserve St. Louis, Macrotrends Data as of June 2026.

Public Markets Rates

Inflation: Headline Pressure Builds Again

Headline CPI rose to 4.2% in May 2026, up from 3.8% in April, marking another move away from the disinflation trend. The increase was mainly driven by energy and food prices tied to geopolitical and supply disruptions, while core CPI remained more contained at 2.9%. Underlying demand pressure is not accelerating aggressively, but repeated external shocks are making it harder for inflation to fall cleanly back toward target.

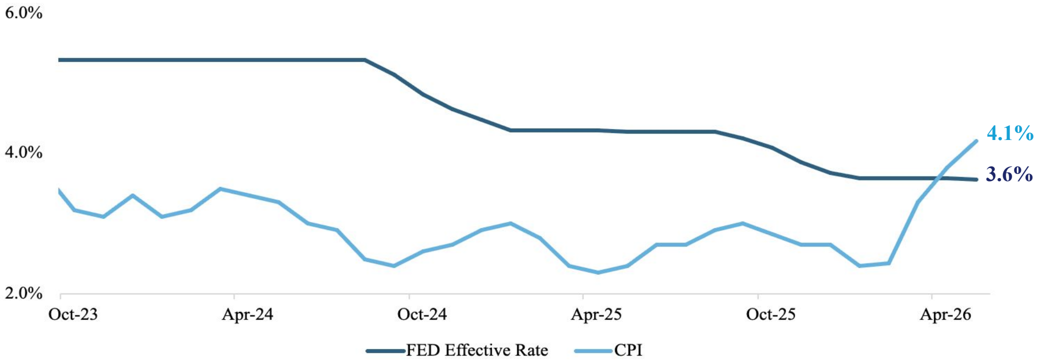
The Fed: Still on Pause, With Less Room to Ease

With inflation moving higher and the effective fed funds rate sitting around 3.6%, the Fed has less flexibility to cut rates in the near term. The market is no longer just debating when easing begins, it is questioning whether cuts are appropriate at all while headline inflation is reaccelerating.

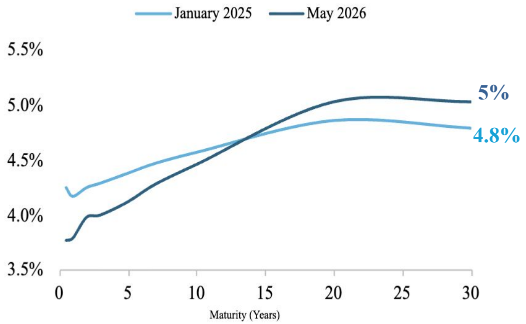
Yield Curve: Higher-for-Longer Still Being Priced In

The yield curve continues to price a higher-for-longer rate environment. The long end remains elevated, with the 10-year Treasury around 4.5% and the 2-year remains close to 4.1%. That positive term spread reflects investors demanding more compensation for duration risk, inflation uncertainty, fiscal pressure, and geopolitical risk. This is not a recessionary curve signal; it is a market pricing in a longer period of elevated capital costs.

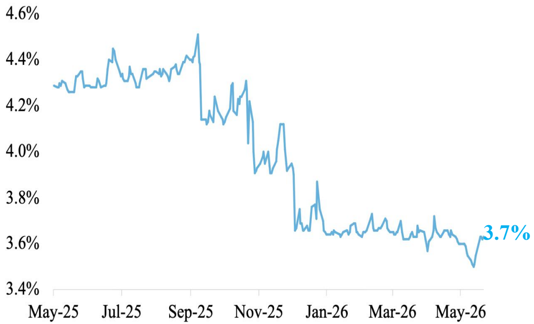
CPI vs. Fed Effective Rate



Treasury Yield Curve

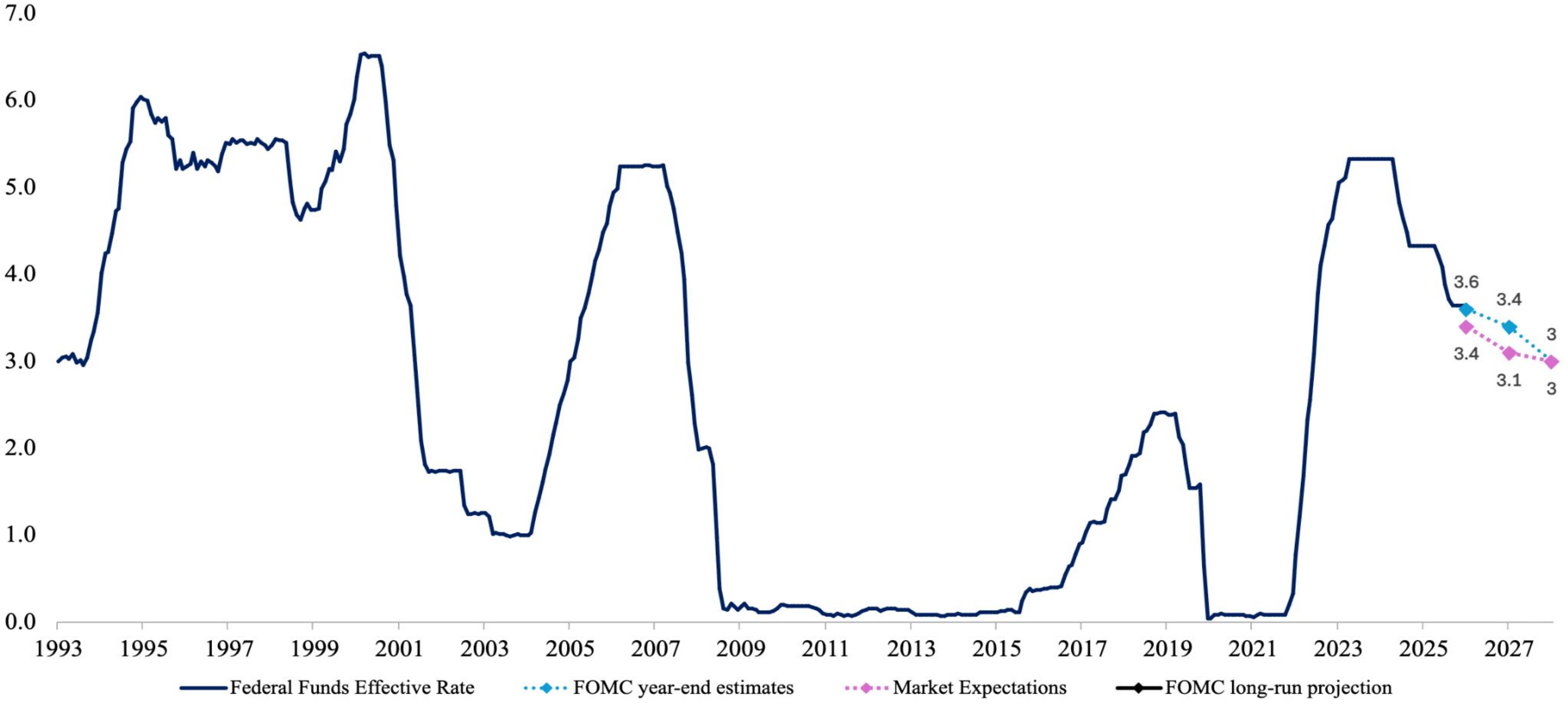


US SOFR Overnight Rate



Sources: Federal Reserve St. Louis, U.S. BLS, U.S. Dept. of Treasury, CME FedWatch, June 10th 2026.

Fed Funds Rate Expectations



Sources: Federal Reserve St. Louis, Bloomberg, June 10th 2026.

Public Credit Markets

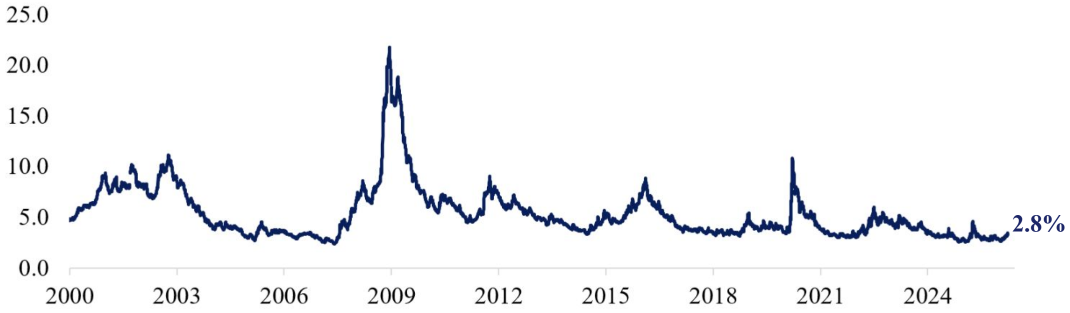
Spreads: Wider but Not Worrying

High-yield credit spreads have narrowed back to around 2.8% in Q2 2026 from roughly 3.16% in Q1, reversing the geopolitical-driven widening earlier in the year and returning to the low end of their post-crisis range. The move reflects the fading of sector-specific repricing rather than any shift in broad credit fundamentals; spreads in manufacturing, industrials, and chemicals stayed comparatively resilient.

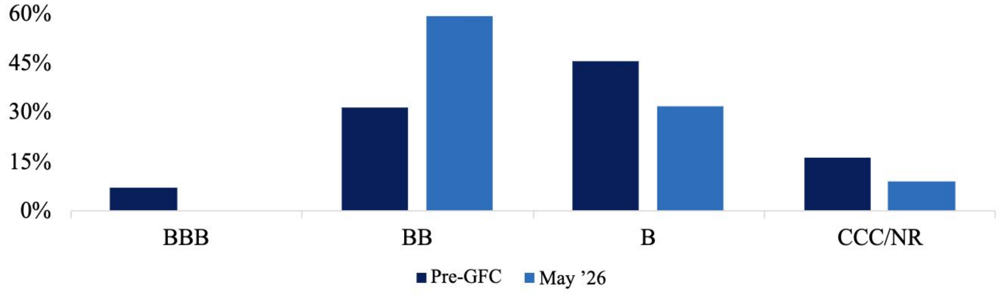
Credit Quality: A Structurally Stronger Index

The high-yield index is better positioned than in prior cycles. BB-rated bonds now account for 59% of the index, with CCC and below exposure at just 8.8% meaningfully less tail risk than heading into the last two downturns. Corporate balance sheets remain healthy, debt-servicing capacity is intact, and the labor market continues to provide a floor under credit performance. That structural cushion provides meaningful downside protection if macro conditions soften.

US Corporate High Yield Average Option Adjusted Spreads (%)



Credit Rating Weights in US High Yield Index



Source: Federal Reserve Bank of St. Louis, J.P. Morgan Domestic High Yield Index weights.

Bank Lending Markets

Bank Balance Sheets: Flush but Cautious

Banks remain well-capitalized and liquid. The loan-to-deposit ratio is holding near 72%, leaving an estimated $1 trillion of untapped lending capacity across the system, and Tier 1 capital sits at roughly 14% of assets, comfortably above regulatory minimums. The capacity to lend is clearly there; what's missing is appetite, not ability.

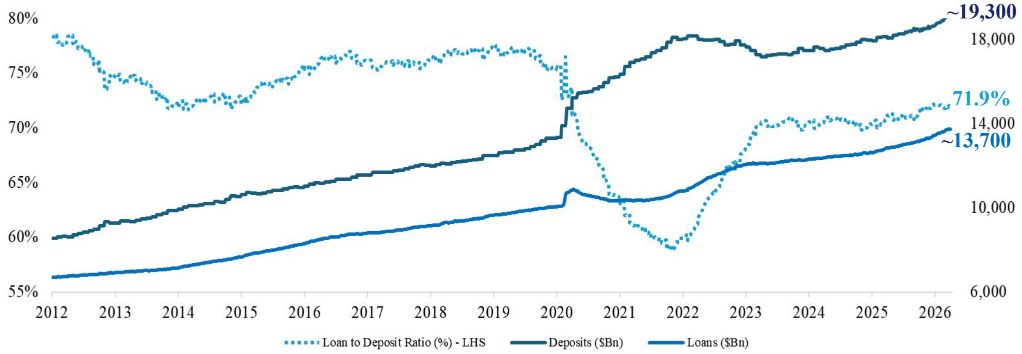
Lending Standards: Tightening at the Margins

The Fed's latest Senior Loan Officer Survey (April 2026) showed banks still tightening C&I standards on net, pointing to a softer economic outlook, industry-specific worries, and lower risk tolerance. Commercial real estate standards were little changed, and loan demand was flat-to-weaker across the board. Tellingly, banks also tightened terms on lending to nondepository financial institutions, a sign the caution is spreading beyond conventional corporate credit into the wider funding ecosystem.

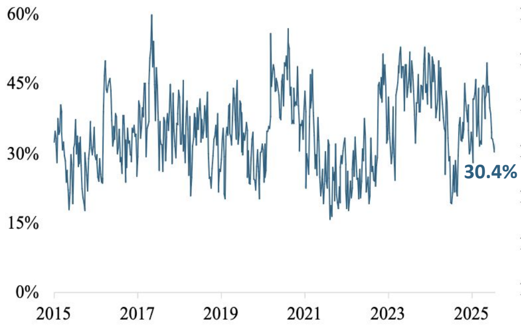
Sentiment: Improving, but Not Yet Bullish

Lender sentiment has come off its spring highs leaving it moderate rather than buoyant. Banks are positioned to deploy capital and are doing so selectively, concentrating on borrowers with strong credit quality. The posture is cautious engagement rather than retrenchment, consistent with a late-cycle backdrop.

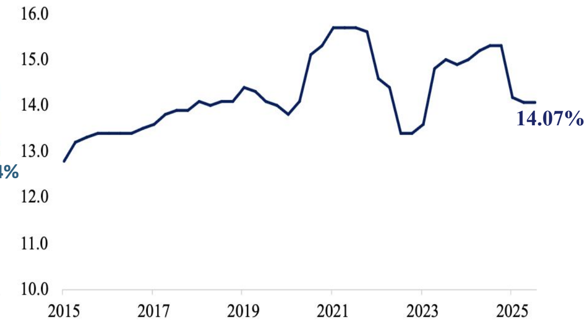
Loan to Deposit Ratio



Lender Sentiment Survey, % Bullish



Bank Tier-1 Capital as % of Assets



Sources: Federal Reserve St. Louis, S&P Capital IQ, AAII.

Private Credit Markets

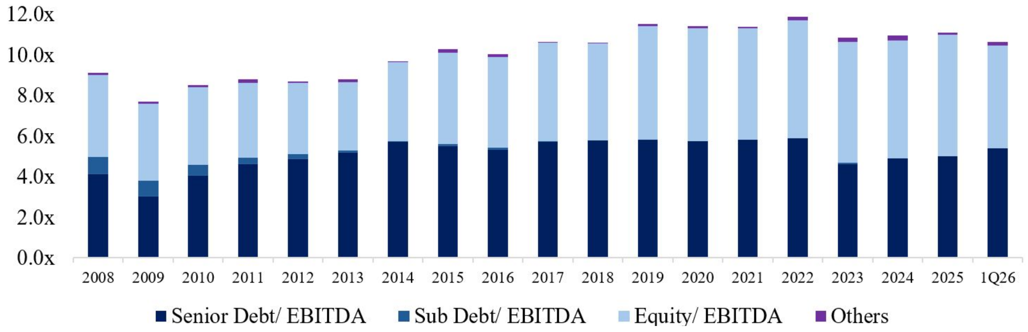
LBO Multiples: Holding Firm

LBO purchase-price multiples have stayed remarkably steady, holding in the 10.0-10.5x EBITDA band from 2024 through 2025 and into Q1 2026 even as rates remained elevated. Senior debt still makes up roughly 4.5-5.0x of the capital structure, and sponsors are closing the rest with bigger equity checks, a sign of continued conviction in the quality of the assets they're buying.

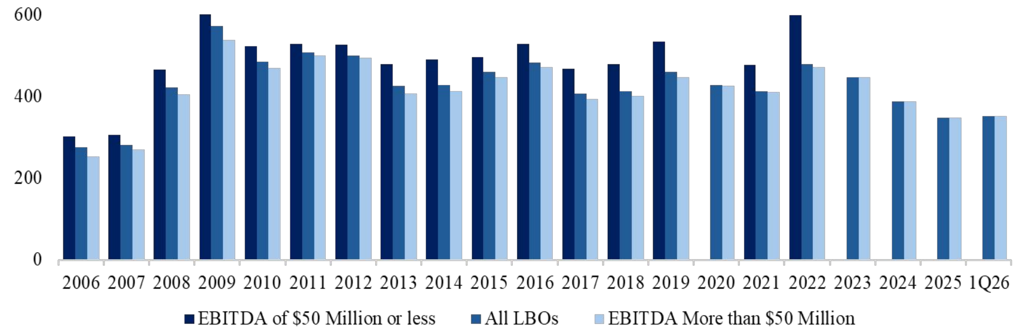
Spreads: Compression Continues, but Bifurcated

The long-run compression in spreads is still intact: all-in institutional spreads have fallen from around 600bp in 2022 to roughly 350bp in Q1 2026, led by larger, higher-quality EBITDA borrowers, where spreads tightened from 446bp in 2023 to 352bp in Q1 2026 as lenders competed harder. Beneath that average, though, the market is splitting K-shaped, B-minus spreads widened nearly 70bp in Q1 and loan prices fell 184bp on the quarter, as tariff uncertainty, geopolitical risk, and AI-driven repricing of software credits hit the lower end. M&A-related loan volume still hit $51.2 billion, a four-year high, even as total institutional volume ran 23% below a year earlier. Sponsors remain hungry for well-structured deals, but pricing discipline and credit selection are increasingly what separate winners from the rest.

LBO Purchase Price Multiples (EBITDA Multiples)



LBO Institutional Spreads



Source: Pitchbook.

M&A Trends

Deal Flow: Loudest quarter on record

In Q1 2026, global M&A dealmakers powered through geopolitical headwinds, from trade policy uncertainty and AI disruption risk to armed conflict and energy inflation, to drive a historic level of activity. Total deal value reached an estimated $1.6 trillion, up 8.8% QoQ and 50.6% YoY, a new quarterly high in our data series. The total was weighted toward the upper end of the market and included the largest single transaction on record (xAI's acquisition). Deal count came in at an estimated 13,877 transactions, up 18.3% YoY and landing at the same record levels we saw in Q4, underscoring the strength of the M&A market.

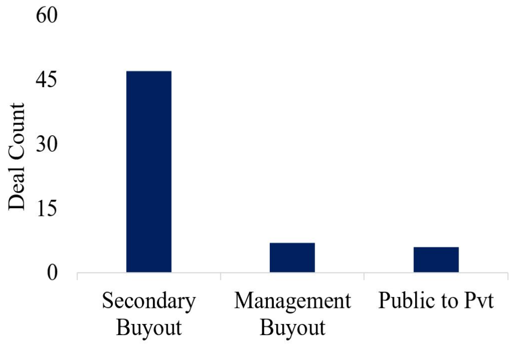
Deal Mix: Conventional, but Disciplined Deployment

The mix shows capital moving through tried-and-tested structures rather than chasing novelty. Conventional M&A (714 transactions) and primary buyouts (464) make up the bulk of activity, while 335 add-on deals underline how committed sponsors remain to buy-and-build as a way to scale. Sponsor-backed buyers accounted for roughly 40% of global deal count and 50% of total value in Q1, a reminder of how central private equity has become to this cycle. The picture is one of mature, deliberate deployment - not a fleeting window.

Global M&A Activity

Core Deal Types by Count

Other Deal Types by Count



Source: Pitchbook.

Outlook

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H2 2026 Outlook: Economy and Deal Landscape Remain Constructive

The foundation heading into the second half of 2026 is firmer than the headline risks imply. Growth is steadying, GDPNow has Q2 tracking near 3.3% after a 1.6% Q1 with a generational AI capex cycle driving private investment and corporate profitability still robust. The labor market is balanced, credit conditions are sound, and capital markets are open and active.

The main wildcards are external, and energy is the biggest. Oil's surge is the most direct threat to the inflation path and therefore to the Fed's timeline. Headline CPI has already climbed to 4.2%, a three-year high, even as core inflation stays comparatively contained near 2.9%. If the energy shock proves transitory and core continues to behave, the door to easing reopens and deal activity should reaccelerate later in the year; if energy pressures persist and bleed into structural inflation, a higher-for-longer regime gets entrenched, compressing multiples and tightening financing further.

The base case stays constructive: a stable macro backdrop, a Fed that is on hold but not hostile, now under new chair Kevin Warsh and a sharply divided committee record dry powder hunting for deployment, and a deal pipeline that is paused, not broken. The pull-forward of Q1 megadeals leaves a temporary air pocket, but the structural engines of M&A sponsor liquidity, strong corporate balance sheets, and the need to reposition portfolios around AI, the energy transition, and supply-chain resilience remain firmly in place.

Richard Consul, CFA

Founder & Managing Partner

Mr. Consul brings more than 20 years of experience in domestic and international capital markets as a Senior Portfolio Manager and strategist across fixed income, currencies, and commodities. Most recently, he served on Victory Capital's institutional fixed income team and investment committee, overseeing nearly $7 billion in assets across Total Return, Short-Duration, and Convertibles strategies. Throughout his career, he has partnered with corporate, banking, and insurance clients to address complex challenges related to liquidity, risk management, asset-liability management (ALM), and secondary market dynamics.

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Mitch Vermet, CFA, CAIA

Partner & Managing Director

Mr. Vermet brings nearly a decade of experience in institutional asset management and investment banking. He has been part of investment teams responsible for portfolio construction and tactical asset allocation of more than $30 billion in institutional capital, supporting clients in managing balance sheets through strategic asset liability management solutions. As a trusted advisor, Mitch helps clients address immediate challenges while prudently managing risk and positioning portfolios to capitalize on opportunities across evolving macroeconomic environments.

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