

Banks Are Pulling Back: What Private Credit Funds Need to Know Now

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KEY POINTS

- Major U.S. banks have raised back-leverage spreads to as much as 200 basis points over SOFR, up from roughly 175–180 basis points.
- Banks are tightening concentration limits on software, technology and health care loans amid AI disruption concerns for SaaS business models.
- Non-traded BDC redemption requests surged to 4.8% of net asset value in Q4 2025, prompting Moody's to revise its BDC sector outlook to negative.
- The FSB, SEC and federal banking regulators are all increasing scrutiny of private fund leverage simultaneously.
- Fund managers should diversify leverage sources, stress-test borrowing base structures and negotiate stronger cure-period protections now.

For the first time in private credit's growth era, the banks that fueled its rise are tightening the terms on which they lend. Since late 2025, major U.S. banks have been raising the cost of back-leverage, the credit arrangements through which private credit funds borrow against their loan portfolios via a special purpose vehicle (SPV), and imposing more restrictive terms on those facilities. Spreads have climbed from approximately 175–180 basis points (bps) over SOFR to as much as 200 bps, with the Financial Stability Board (FSB) separately benchmarking fund portfolio financing at approximately 225 bps over benchmark rates. Three converging forces are driving this shift: concerns over AI sector valuations, rising business development company (BDC) redemptions, and heightened regulatory scrutiny. Private credit fund managers and BDC sponsors who act now will be better positioned than those who wait.

BACKGROUND

Back-leverage is a financing mechanism in which a private credit fund or BDC borrows from a bank using its existing loan portfolio as collateral, typically through an SPV that holds a pool of loans and borrows against them under a borrowing base structure. The borrowing base is a formula the bank sets by applying haircuts based on loan riskiness and sector concentration limits. If the amount drawn ever exceeds the borrowing base, the fund faces a deficiency that must be cured quickly or an event of default results. Prior to the recent tightening, typical terms included pricing of approximately 175–180 bps over SOFR and advance rates in the 60–70% range.

WHAT IS CHANGING

Since the second half of 2025, major U.S. banks have been resetting back-leverage terms across five categories:

Pricing Increases. Spreads on back-leverage facilities have widened from approximately 175–180 bps over SOFR to as much as 200 bps, according to Reuters. For leveraged funds, even a 20 bps increase is substantial. The FSB's May 2026 report separately benchmarked fund portfolio financing at approximately 225 bps over benchmark rates, signaling that regulators are actively tracking these pricing levels.

Lower Advance Rates and Tighter Concentration Limits. Banks have been reducing advance rates on loans in certain sectors, with some major banks reporting rates generally in the 60–70% range, while tightening sector concentration limits, particularly for software, technology, and health care loans. Concerns center on whether recurring-revenue SaaS business models can withstand AI disruption. Software and SaaS represent approximately 25% of BDC portfolios on a median basis according to Moody's, and roughly 19% of total direct loans, according to BIS, making these sectors a focal point for banks reassessing collateral quality.

Enhanced Reporting and Reduced Bank Appetite. Lenders are requiring more frequent portfolio reporting, including mandatory payment-in-kind (PIK) conversion notifications and tighter borrowing base certification requirements. Meanwhile, the universe of willing lenders has narrowed: according to Bloomberg, executives at major banks were privately discussing short-term pauses on new leverage lines. Fewer active lenders mean less competition, and the banks that remain can afford to be more selective.

WHAT IS DRIVING THE TIGHTENING

Three converging pressures are behind the shift. First, non-traded BDC redemption requests surged to 4.8% of net asset value (NAV) in the fourth quarter of 2025 (up from 1.6% in the third quarter), with Moody's subsequently revising its BDC sector outlook to negative in April 2026. Second, regulatory attention is intensifying: the FSB identified fund portfolio financing as a key vulnerability channel, the Securities and Exchange Commission's (SEC) 2026 examination priorities target private fund leverage, and new Federal Reserve/Federal Deposit Insurance Corporation (FDIC) disclosure requirements effective December 2024 now make bank exposure to private credit more visible to supervisors. Together, these signals give banks reason to tighten terms proactively rather than wait for regulators to demand it.

WHAT FUND MANAGERS SHOULD DO NOW

1. **Model the cost impact.** A 20–25 bps increase in back-leverage pricing, applied to a typical 1.0x–1.5x leverage ratio at the SPV level, translates to roughly 20–37.5 bps of additional drag on unlevered portfolio returns. Update return projections and limited partner (LP) reporting accordingly.
2. **Review borrowing base eligibility.** Tighter concentration limits and higher haircuts on technology or health care loans can quietly reduce available leverage. Know exactly what triggers a borrowing base deficiency in your facility documents and ensure sufficient liquidity buffers are in place.
3. **Negotiate cure periods and deficiency mechanics.** Ensure facility documents include adequate cure periods (ideally 15–30 days rather than immediate) and flexible cure mechanisms such as capital contributions, loan sales, or substitution of eligible collateral.
4. **Diversify leverage sources.** Evaluate whether rated note feeders, collateralized loan obligation (CLO) structures, or private credit-on-private credit solutions can supplement or replace bank back-leverage in the capital stack.

5. Prepare for enhanced reporting. Getting ahead of lender demands on PIK status, EBITDA add-back detail, and sector concentration puts managers in a stronger negotiating position at renewal.

Private equity sponsors should also note that if a fund's private credit lender faces tighter back-leverage constraints, that lender may reduce capacity or become less willing to extend new commitments, fund delayed-draw term loans, or approve amendments. Maintaining relationships with multiple credit providers is advisable.

LOOKING AHEAD

The [FSB's four announced workstreams on private credit vulnerabilities](#), the [SEC's 2026 examination priorities targeting private fund leverage and valuations](#), and [Moody's negative BDC sector outlook](#) all suggest the current tightening is structural rather than temporary. Managers who diversify leverage sources, maintain strong lender relationships through transparency, and stress-test their borrowing base structures now will be better positioned than those who wait for conditions to stabilize on their own.

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