

M&A Stays Big

Private Equity 2026 Midyear Outlook

MARKET INSIGHTS | 2026 MIDYEAR OUTLOOK | PRIVATE EQUITY | July 2026

“The foundation for a multi-year recovery is now in place. The next phase depends less on direction than on breadth.”

Key Reflections

In a replay of 2025, the first half of 2026 featured increasing macro volatility, but instead of a trade war we had a Mideast war. Volatility usually creates a chill in M&A activity by driving prospective buyers to the sidelines. And while that was the case for PE buyout activity, where deal value tracked flat to slightly down for the year, total M&A surprised on the upside. The announced value of deals has risen 17% year-to-date.¹ That follows a 44% surge during 2025 and places the recovery well above the 16% growth trend line that we extrapolated at the beginning of the year (*Display 1*).

While confirming our “higher for longer” M&A thesis, our expectation for a broadening across PE has not yet come to pass. At the current midpoint of what we believe will be a 5+ year M&A cycle, PE deal flow has yet to fully ignite. The pace of capital deployment remains constrained compared to buying power. And nowhere is that relationship more stretched than in the middle market, where a full unlocking of capital implies a 20% or more increase from current levels (*Display 2*).

What We Are Seeing

Strong M&A markets matter because private equity traditionally participates in nearly half of all deal activity, either as a buyer or a seller. Improving transaction activity supports exits, distributions, fundraising and ultimately new investment activity. However, that participation rate has dropped to under 31% for the first time in ten years, highlighting the extremely deliberate

AUTHORS



DAVID MILLER
Managing Director,
Global Head of Private
Credit & Equity



TIM CLARKE
Executive Director
Head of Private Credit
& Equity Research

¹ Source: Dealogic, Morgan Stanley Research. As of June 23, 2026.

pace among both PE buyers and sellers.² Much of the resurgent strength in M&A is driven by mega-transactions led by strategic buyers that have been unbridled by an easier antitrust backdrop, while middle-market volumes have grown only modestly. We believe that a broadening of activity in the small and mid-sized market is still a matter of when and not if, especially as macro volatility subsides in the second half of the year and more certainty is gained regarding inflation and future interest rates.

While smaller private companies have been slow to transact, a new opportunity is taking shape for late-stage growth investing in private companies that are valued above \$1 billion, or so-called 'Unicorns.' Year to date, the capital flowing to late-stage private companies that have received six or more rounds of VC-financing has skyrocketed to 74% of all proceeds raised compared to a 10-year average of 25%.³ After significant turnover, a new generation of private Unicorns has emerged that are scaling revenue and creating value at breakneck speed. Many are on the leading edge of AI or are rapidly adopting AI to accelerate earnings growth. Most are opting to stay private for longer, shifting even more value creation into the private and pre-IPO phase of a high-growth company's life cycle.

What We Are Doing

Our investment focus remains centered on management teams and companies that are creating value operationally rather than relying on financial leverage or an arbitrage between buying and selling multiples. AI is becoming an increasingly important differentiator across our portfolio companies, with applications spanning customer service, software development, pricing, procurement and operational

efficiency, and we are actively provisioning them with the tools and best practices they need. AI initiatives have moved beyond the pilot phase to meaningful use cases and we expect meaningful outcomes by year end.

In our late-stage growth strategy, we are actively deploying capital into category-leading private companies that combine public-company quality with venture-like growth. We are using Morgan Stanley's sourcing advantage to access periodic fundraising rounds conducted by these companies, as well as the firm's experience in underwriting AI to discern between industry winners and losers.

What We Are Watching

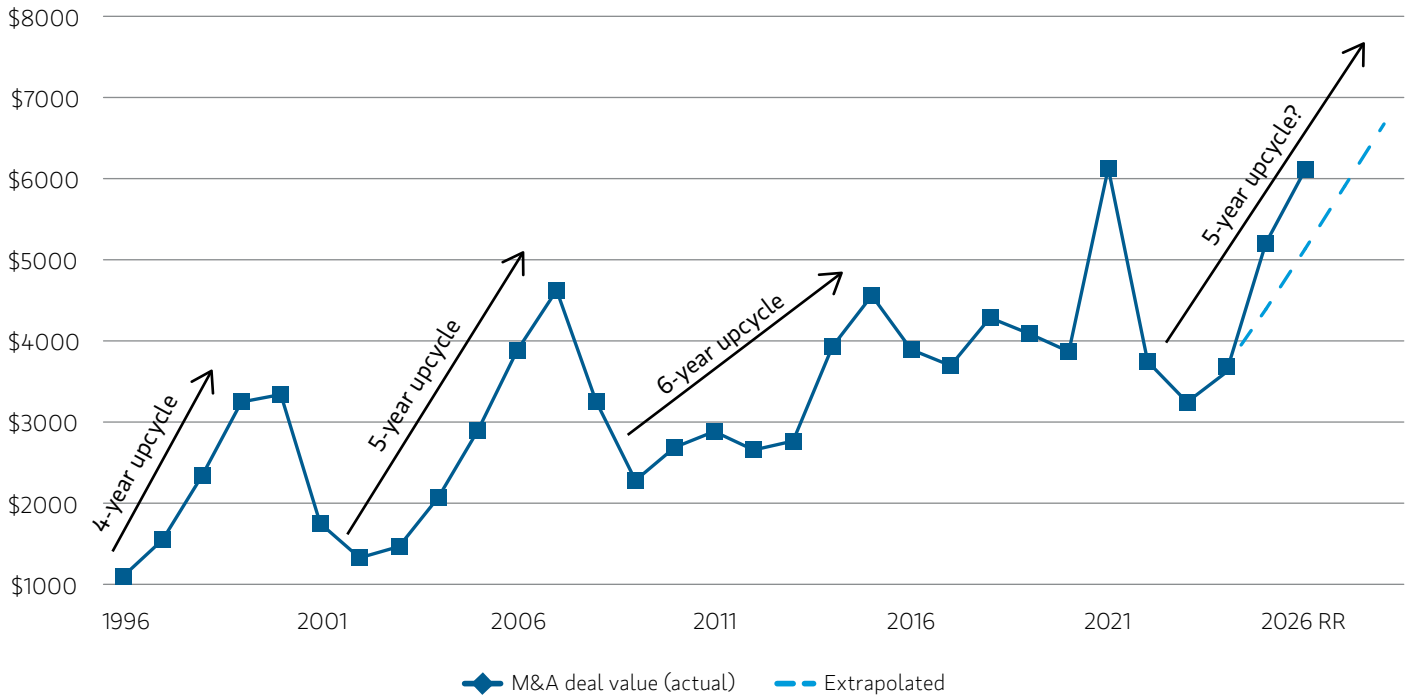
We remain constructive on the middle market. The PE acquirer is more interest rate sensitive than other M&A participants, and the pause in Fed rate cuts and the resurgence in core inflation slowed deal flow as a result. However, we view those factors as a temporary byproduct of macro volatility that will likely subside in the second half of the year, paving the way for a more benign backdrop that re-ignites the PE deal engine. A deterioration in the monetary outlook that results in rate hikes rather than cuts following a Fed pause is what we are watching very closely.

We are also monitoring valuation discipline. High-quality assets continue to command premium prices, making manager selection and underwriting increasingly important. Finally, we remain focused on the pace of AI adoption, evolving trade and regulatory policy, and the durability of earnings growth. If these factors remain supportive, we believe that private equity is well positioned to enter the next phase of a longer-duration expansion.

² Source: PitchBook Data, Morgan Stanley Investment Management. As of March 31, 2026.

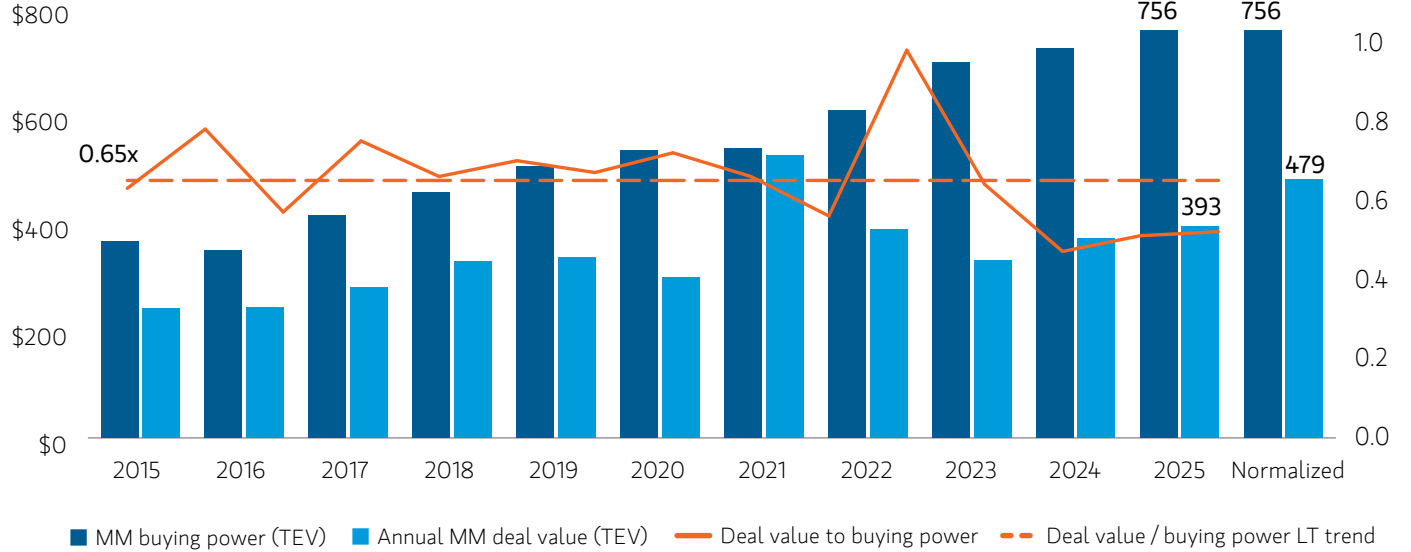
³ Source: PitchBook Data. As of March 31, 2026.

DISPLAY 1
Global M&A Deal Value (\$B)



Source: Dealogic, Morgan Stanley Research. As of May 31, 2026. Extrapolated is for illustrative purposes only and assumes 12% trendline growth from 2026 through 2028.

DISPLAY 2
Private Equity Middle Market Buying Power (\$B)



Source: PitchBook LCD, Morgan Stanley Investment Management. As of March 31, 2026. US only.

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