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# Uncertainty in Private Equity Markets: Inflation, Tariffs and Regulatory Changes



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## Introduction

Private equity (PE) sponsors in the United States enjoyed a number of years of ever-increasing success, whether measured by fundraising, number of acquisitions, exit multiples or return on capital. Low inflation, low interest rates and a generally pro-growth government policy were the tailwinds that drove this growth. Deal-making continued at a rapid clip through the beginning of the COVID era.

Eventually, inflation, rising interest rates and other economic factors caught up with the PE industry and deals decreased in 2023 and 2024, and appear to be decreasing even more in 2025 (note this chapter is only being written in July 2025). Government policy became increasingly mixed, as geopolitical tensions and internal politics caused many to rethink long-held beliefs about the economy and business.

At the time of writing, the most striking difference from the boom era of PE deal-making is not one specific issue, but instead the sheer number of issues facing dealmakers. With so much uncertainty, finding attractive targets and developing reliable valuations that encourage sellers to transact while also allowing PE sponsors to achieve a meaningful return is a tall order to say the least. The multivariate analysis has many opportunities to go wrong, and for now is encouraging many buyers and sellers to wait and see what the world will bring. It is unclear at what point the uncertainty will ebb, or, if it does not, at what point (if ever) sellers will accept the lower resulting valuations.

We have attempted to give the reader a high-level review of the key areas of uncertainty that PE sponsors have to address in today's market, and how they look at them.

## Inflation

Inflation continues to be a dominant theme in 2025. While inflation itself has tempered significantly since the high rates of inflation of 2022 and 2023, the market has been on the lookout for inflation stemming from the tariff regime introduced by President Trump. While signs of inflation have appeared in certain economic measures, to date, widespread inflation has not materialised.

More important than the actual inflation, though, is the fear of inflation. The nature of the tariff regime is such that it is unpredictable, and not clearly tied to any particular guiding principle or measurement. As a result, even if there is no significant inflation from the tariffs that have been introduced to date, since the market does not know if or when additional tariffs will be adopted and how other countries will react to those tariffs, buyers are forced to underwrite a wider range of possible outcomes. This increase in potential end results, and

related uncertainty, puts further pressures on sponsors as they diligence prospects and ultimately make offers for businesses.

Sellers do not have much leverage to push back against this concern, as the tariffs are an exogenous shock that is as unpredictable for sellers as it is for buyers. Some sellers have been willing to accept lower valuations. The most frequent result, however, is sellers sitting it out until the tariffs are finally settled (although no one really knows when this will be). This uncertainty has also resulted in a greater willingness by sellers to accept earnouts, so that buyers and sellers can share the risk of tariffs (and the business generally). While this at least allows transactions to occur, in some ways it just pushes uncertainty further down the road, as sellers continue to be indirectly invested in the business they sold.

## Interest Rates and Monetary Policy

Inflation rates continue to be a material source of uncertainty for PE transactions in the United States. While most central banks have materially lowered interest rates, the Federal Reserve has taken a circumspect approach, perhaps because of the significant criticism it received for not raising interest rates fast enough in the face of the inflation of 2022–2023. On top of this, President Trump has criticised the central bank, particularly Chairman Powell, for not lowering interest rates quickly enough. Nonetheless, the Federal Reserve has been focused on its dual mandates of managing inflation and the labour markets.

Given that floating rate debt is one of the primary costs of capital for PE sponsors, it is clear to see how this creates a level of uncertainty in the deal-making process. While PE sponsors may model lower interest rates in the future, they must be prepared for interest rates to stay the same (or potentially rise, if inflation surfaces from the tariffs discussed above). This further widens the potential outcomes that sponsors need to model, making it more difficult to come to agreed valuations.

## Artificial Intelligence (AI)

The rapid rise of AI, and in particular generative AI, is a development that everyone agrees will change most, if not all, aspects of the economy. How and when that will occur, however, is still unpredictable and unknown. As a result, acquirers have had to rapidly incorporate this uncertainty into their deal underwriting. On the positive side, it is clear that AI can bring significant savings to a PE sponsor's portfolio, as well as the due diligence process itself. AI has been adopted by PE sponsors and their portfolio companies at a rapid clip that is expected to continue. But AI can also displace incumbent offerings in an industry, or an entire industry. PE sponsors



cannot know the rate at which AI will improve, in which direction it will go and how widely it will be adopted. As a result, it is an additional challenge in an already challenging environment (although a great opportunity as well).

## Regulatory Changes

The Trump administration has changed the paradigm on regulation in the United States. Almost every regulatory regime is undergoing significant re-consideration, and some are being wiped out entirely.

One need merely review the trajectory of Environmental, Social and Governance (ESG)-driven investing. Previously, ESG was a focus for almost every PE sponsor, with most required to provide an ESG review for each portfolio company and provide reports of the same to its limited partners. Other PE sponsors went even further, with ESG-driven investment mandates. Now, ESG is getting significant pressure from both the President and the U.S. Securities and Exchange Commission (SEC), with many companies removing references to it on their websites and marketing materials.

Although this chapter is not going to summarise every regulatory change, the key point remains the same: significant changes are happening in unpredictable and uncoordinated ways. While this might provide chances for upside in the long run, investing in any heavily regulated industry is difficult given the unpredictable nature of government action. Investors in energy, telecommunications and pharmaceutical industries must be wary of the sea-changes that their industries are undergoing and react accordingly.

Even in non-regulated industries, these changes in regulation can be meaningful. For example, as noted above with respect to AI, it is unclear if the government will take a meaningful role in the regulation of AI, or whether the states will step in and fill that role.

## Geopolitical Tensions

Geopolitical uncertainty remains a significant concern for PE investors in 2025. Ongoing tensions in Eastern Europe, volatility in the Middle East and trade disputes between major economies like the United States and China create risks that can disrupt supply chains, impact asset valuations and alter cross-border deal-making.

PE firms increasingly incorporate geopolitical risk assessments into their due diligence processes. Deals involving cross-border transactions may require additional scrutiny, particularly in industries subject to tariffs, export controls or foreign investment restrictions. Meanwhile, firms are also exploring geographic diversification to mitigate exposure to political instability.

## Deal-Making Environment in 2025

The deal-making environment in 2025 remains challenging, defined by valuation uncertainty and reduced transaction volumes. Rising interest rates, inflation concerns and unpredictable tariffs have widened gaps in expectations between buyers and sellers. Sellers often resist lower valuations, while buyers remain cautious about overpaying in a volatile market. Many participants are delaying transactions, waiting for greater economic stability. To address these challenges, earn-outs, deferred payments and structured equity have become critical tools for bridging valuation gaps and sharing risks. These mechanisms allow deals to proceed while mitigating uncertainties for both parties.

Sector performance has become increasingly polarised, with some industries thriving while others struggle. Technology, healthcare and renewable energy remain standout winners due to their resilience, scalability and alignment with global trends. AI is driving operational efficiencies and scalability in technology, while healthcare benefits from consistent demand and medical innovation. Renewable energy is bolstered by global decarbonisation efforts and supportive policies. However, sponsors must carefully assess whether valuations in these sectors remain sustainable amid growing competition.

Conversely, traditional manufacturing, fossil fuels and retail face mounting pressures. Manufacturing continues to grapple with supply chain disruptions and geopolitical instability, though opportunities may exist in advanced manufacturing and robotics. Fossil fuels are under scrutiny from shifting energy policies and declining demand, but transitional technologies like carbon capture or natural gas infrastructure may offer potential. Retail faces headwinds from evolving consumer preferences and e-commerce dominance, yet innovative, experience-driven models could hold promise. Sponsors must weigh sector dynamics carefully to avoid pitfalls and identify overlooked opportunities.

Creative deal structures have evolved to address these uncertainties. Earn-outs allow sellers to remain invested in the future success of the business, while deferred payments provide buyers flexibility by reducing upfront financial strain. Structured equity has also emerged as an effective solution for balancing risk and reward. These tools help sponsors navigate valuation challenges while enabling transactions to move forward despite economic volatility.

Despite the hurdles, PE sponsors are adapting by targeting resilient sectors and leveraging innovative deal structures. By embracing flexibility and focusing on long-term trends, sponsors continue to pursue meaningful value creation in a complex environment.

## Exit Landscape and Portfolio Management

The exit landscape in 2025 reflects the broader challenges facing PE sponsors. The initial public offering (IPO) market remains subdued as public investors demand robust performance metrics and operational resilience. Fewer portfolio companies are opting for IPOs, shifting focus to alternative exit routes. Strategic buyers have emerged as the dominant option, drawn by synergies and long-term growth opportunities. Financial buyers, however, remain cautious due to valuation uncertainties, pushing sponsors to align portfolio companies with compelling strategic narratives to attract interest.

Extended holding periods are becoming a defining feature of the exit landscape. Sponsors are navigating delayed exits, which heighten performance pressures and demand operational excellence. To sustain value during prolonged ownership, sponsors are prioritising cost optimisation, productivity gains and scalable growth strategies. Technology adoption is also playing a critical role in enhancing efficiency and competitiveness within portfolio companies.

Secondary transactions, such as GP-led continuation funds, are gaining traction as creative solutions to liquidity challenges. These transactions allow sponsors to extend investment timelines for promising assets while offering limited partners liquidity options. By balancing short-term needs with long-term growth potential, continuation funds have become an essential tool for navigating delayed exits.

Sector trends heavily influence exit strategies. Resilient industries like technology, healthcare and renewable energy continue to attract buyers due to their scalability and

alignment with global priorities. Technology benefits from advancements in AI, healthcare thrives on consistent demand and innovation, and renewable energy aligns with sustainability goals. Meanwhile, industries such as fossil fuels, manufacturing and traditional retail face heightened exit challenges. Sponsors targeting these sectors must employ advanced risk management practices, including geographic diversification and scenario modelling, to mitigate exposure and optimise strategies.

Despite these complexities, PE sponsors are finding ways to deliver value through operational improvements, strategic alignments, and innovative exit solutions. Their ability to navigate uncertainties ensures the industry remains a vital driver of value creation.

## Conclusion

The PE landscape in 2025 reflects both challenges and opportunities, showcasing the industry's adaptability and resilience. Valuation uncertainty, lower deal volumes and evolving sector dynamics have reshaped the deal-making environment, requiring sponsors to adopt innovative strategies to bridge gaps and manage risks. Earn-outs, deferred payments and structured equity have become essential tools for facilitating transactions amidst economic volatility. By focusing on resilient

sectors like technology, healthcare and renewable energy, PE sponsors are well-positioned to capitalise on long-term growth opportunities while navigating challenges in more vulnerable industries such as manufacturing, fossil fuels and retail.

Exit strategies have shifted away from IPOs and toward strategic buyers, who are better equipped to leverage synergies and long-term goals in a cautious market. Extended holding periods have heightened the pressure on sponsors to implement operational improvements, optimise costs, and invest in scalable growth strategies to drive sustained portfolio performance. Secondary transactions, such as GP-led continuation funds, have emerged as flexible solutions to address liquidity challenges while extending investment timelines for promising assets.

Despite geopolitical tensions, regulatory unpredictability and macroeconomic instability, PE sponsors continue to innovate and refine their approaches. The ability to adapt to uncertainty, enhance resilience and align investments with future market trends ensures PE remains a critical driver of value creation. In leveraging flexible deal structures and focusing on high-potential sectors, sponsors are not just weathering current challenges but laying the groundwork for sustainable success. The industry's commitment to innovation and resilience positions it to thrive in a dynamic and uncertain environment.



**Adam Rosenthal** helps clients seamlessly execute M&A as well as recapitalisations, joint ventures, co-investments and other corporate transactions. PE sponsors, sovereign wealth funds, pension funds, family offices and other institutional investors routinely look to him for support throughout the life cycle of their portfolio investments.

Adam also advises clients in the financial services industry on the expansion, consolidation and diversification of their businesses, offering workable solutions to complex business, legal and regulatory issues. Adam has represented industry participants across the board, from investment advisers and wealth managers to broker-dealers, private lending platforms and mutual funds.

Outside of the office, you can often find Adam taking a pen to crossword puzzles or putting his tactical skills to work with a game of backgammon. He also enjoys taking road trips with his family.

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**Ryan Miske** is the leader of the firm's worldwide PE practice.

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