IPEM

JULY 6/7/8 2021
CANNES - FRANCE

2021 VISION:

What a difference a year makes!

European private equity has big ambitions for 2021, despite a global pandemic

This 3rd annual survey gauges the mood and outlook of European private equity fund managers for 2021. It was conducted with the support of 16 national private equity associations from France (France Invest), UK (BVCA), Germany (BVK), Switzerland (SECA), Austria (AVCO), Netherlands (NVP), Belgium (BVA), Spain (ASCRI), Portugal (APCRI), Italy (AIFI), Luxembourg (LPEA), Poland (PSIK), Denmark (AOD), Sweden (SVCA), Finland (FVCA) and Norway (NVCA). In total, 223 interviews were completed online from Nov. 18th to Jan. 11th by the CSA institute.

SURVEY CONDUCTED WITH THE SUPPORT OF:

AIFI Italian Private Equity, Venture Capital and Private Debt Association

AKTIVE EJERE ACTIVE OWNERS DENMARK

APCRI

Ascri ASOCIACIÓN ESPAÑOLA DE CAPITAL, CRECIMIENTO E INVERSIÓN

AVCO

BVA

BVCA British Private Equity & Venture Capital Association

BVK German Private Equity and Venture Capital Association

France Invest Association des investisseurs pour la croissance

Pääomasijoittajat Finnish Venture Capital Association

LPEA THE LUXEMBOURG VOICE OF PRIVATE CAPITAL

nvca

NVP Nederlandse Vereniging van Participatiemaatschappijen

PSIK Polskie Stowarzyszenie Inwestorów Kapitałowych

SECA

SVCA

AND BY:

csa CONSUMER SCIENCE & ANALYTICS

When we canvassed the opinion of the European private equity industry a year ago, the mood was distinctly tense. There was a palpable sense that the asset class was pushing its luck with one of the longest bull-runs in history. Add the looming spectre of Brexit and intensifying trade wars, and close to two thirds of market participants feared a worsening business environment.

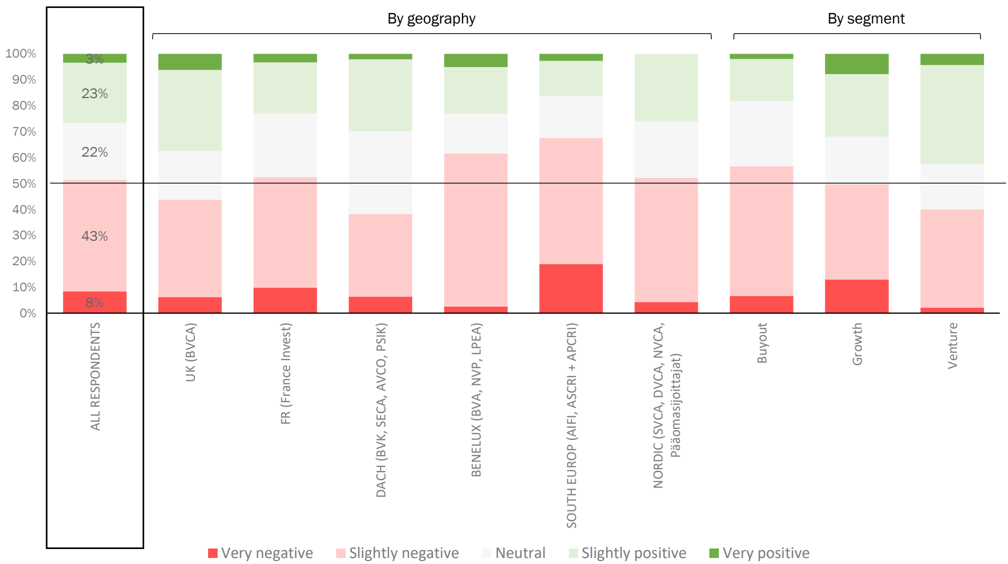
Of course, the change in fortunes, when it came, had little to do with geopolitical infighting and a great deal to do with the virulent ambush of Covid. Indeed, IPEM's third annual survey, conducted by the CSA Institute, in collaboration with 16 national private equity associations, revealed the punishing implications of the pandemic.

Over half of the more than 220 respondents experienced a negative impact on their portfolio *(Exhibit 1)*, with buyouts and Southern Europe, hit particularly hard. Sourcing new opportunities and conducting exits, meanwhile, have been frustrated by a combination of social distancing measures and uncertainty over valuations.

EXHIBIT 1

THE MIXED IMPACT OF THE COVID CRISIS ON PE PORTFOLIOS

How do you assess the impact of COVID-19 on your portfolio?

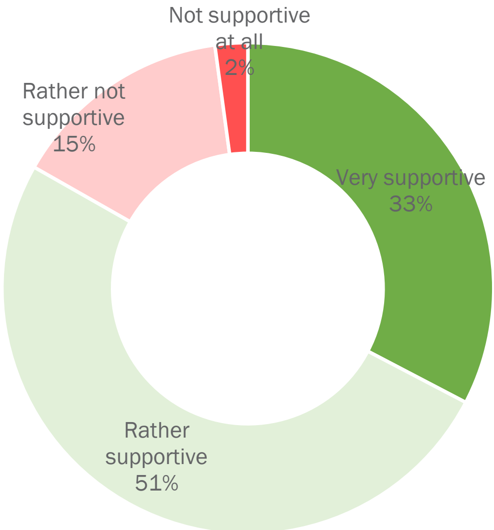


And yet, private equity has once again proved its resilience and ingenuity. So much so, that 27% of survey respondents have experienced positive outcomes from the crisis, rising to 42% in venture capital alone. Furthermore, unprecedented state aid undoubtedly softened the blow for many businesses – indeed, 83% of private equity professionals think their government was supportive of the economy *(Exhibit 2)*, while 71% believe it was supportive of their portfolio.

EXHIBIT 2

EUROPEAN PE IS PRAISING THE ACTION OF GOVERNMENTS DURING THE CRISIS.

For the overall economy, how do you evaluate your national government recovery policies?



GPs in France were the most impressed by their government's response, with a massive 92% acknowledging benefit at an individual investee company level, compared to a solid 78% in the Nordics and 75% in the UK. After initial triaging and emergency liquidity measures were complete, attention quickly reverted to value creation, with over 80% of firms now actively exploring buy and build deals.

"Crucially, a private equity industry that has historically struggled with optics, is also busy positioning itself as part of the global solution," says IPEM Chief Executive Antoine Colson. Over half – 54% – of European GPs believe private equity will become the partner of choice for future recovery policies.

THINGS CAN ONLY GET BETTER?

In fact, the European private equity industry is entering a second year blighted by an international pandemic, considerably more upbeat than at the peak of the cycle. Almost three quarters of GPs expect an improving business environment in Europe over the next 12 months *(Exhibit 3)*. Managers in the Benelux and Nordics are much more positive, while Southern Europeans remain wary.

Of course, managers are not naïve about the challenges they face. A slowdown in economic growth is amongst the industry's biggest concerns, cited by 56% of respondents *(Exhibit 4)*, followed by social unrest and the unrelenting rise of populism. The consequences of Brexit linger on, meanwhile, cited by 49%, rising to 69% for those based in the UK.

The level of sovereign debt has also become a top concern for many GPs, particularly in Southern Europe. And close to 60% of professionals are anticipating increased regulatory and fiscal pressure, rising to 61% for buyout specialists and an overwhelming 87% in the UK.

The biggest challenge facing the European private equity industry, meanwhile, is undoubtedly stubbornly high valuations *(Exhibit 5)*, cited by 89% of respondents. Over half expect to see valuations rise still further in 2021, with 9% expecting valuations to rise significantly, compared to a mere 2% last year.

EXHIBIT 3

EUROPEAN PE EXPECTS A MUCH BETTER BUSINESS ENVIRONMENT IN 2021

How do you expect the business environment to be in 2021 compared to 2020? (In Europe)

> “PRIVATE EQUITY FIRMS ARE PILING INTO A SELECT GROUP OF ‘COVID WINNERS’, WHICH IS INEVITABLY HAVING AN IMPACT ON PRICING,”

EXHIBIT 4

A SLOWDOWN IN GROWTH, SOCIAL UNREST, HIGH VALUATIONS ARE THE TOP CONCERNS OF THE INDUSTRY IN 2021

What are the biggest risks for the European economy and the PE industry in 2021?

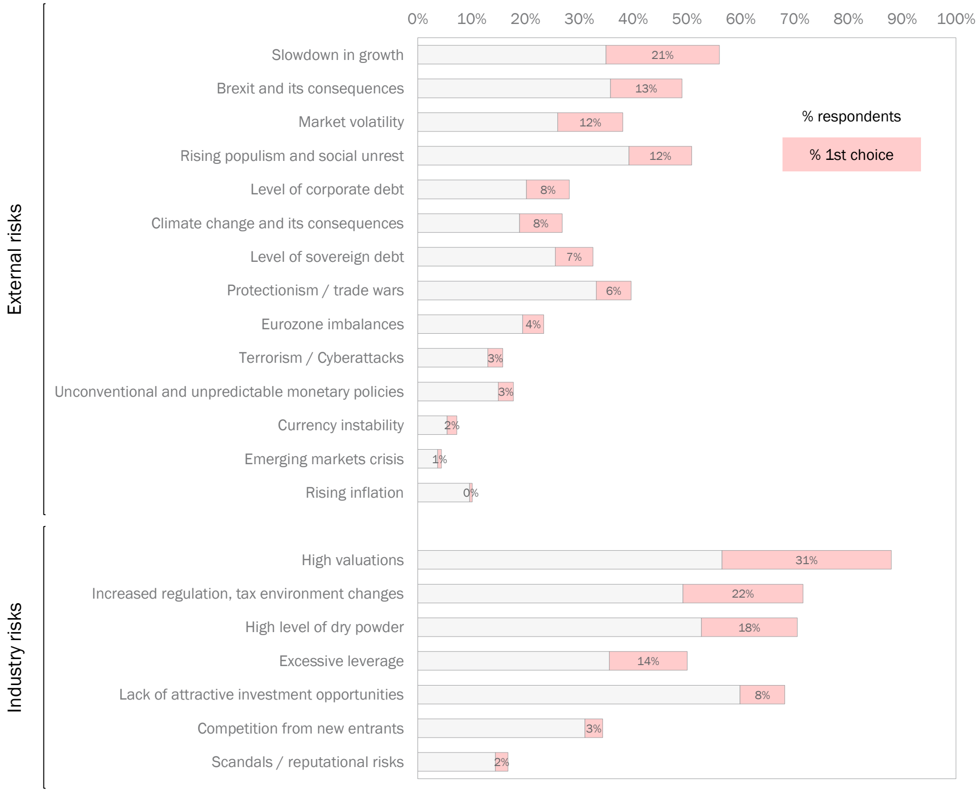


EXHIBIT 5A

THE FOCUSED INTEREST ON COVID-PROOF SECTORS IS PUSHING VALUATION TO NEW HIGHS

What industries do you see as most attractive in your segment in 2021?

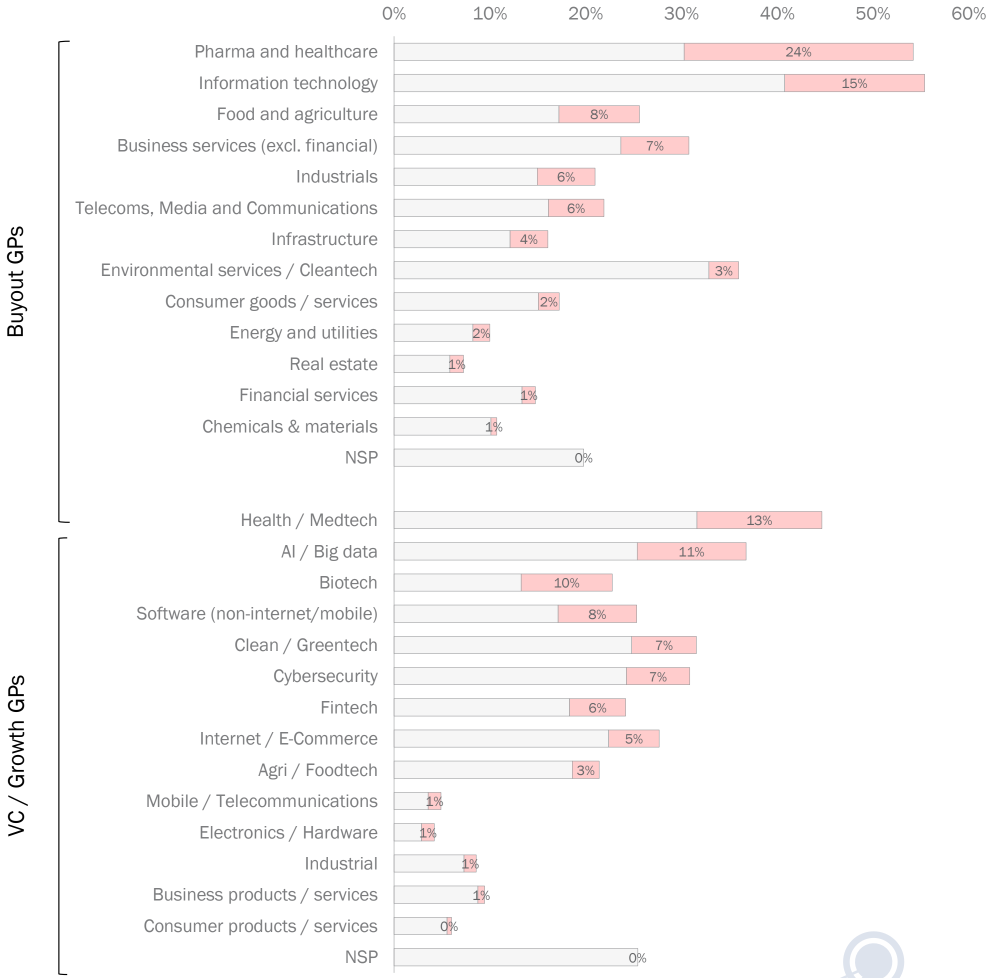
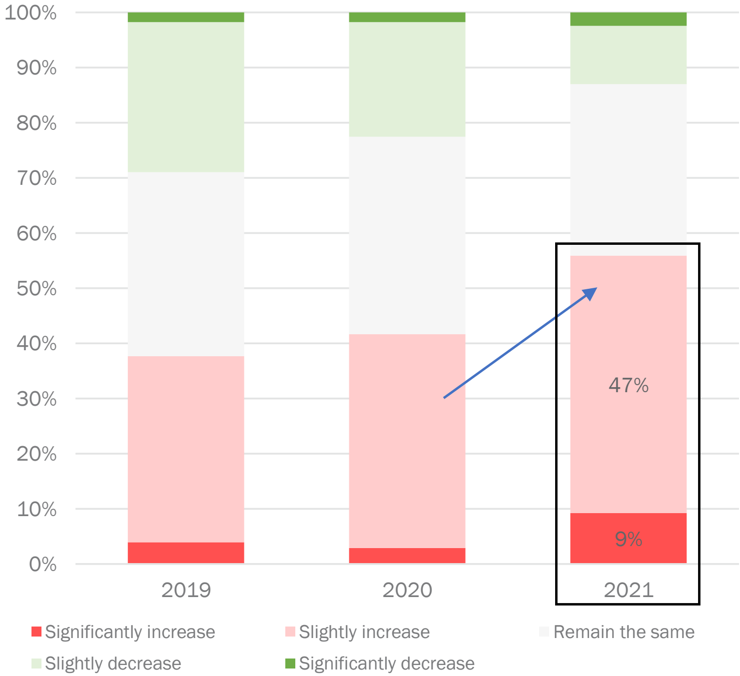


EXHIBIT 5B

THE FOCUSED INTEREST ON COVID-PROOF SECTORS IS PUSHING VALUATION TO NEW HIGHS

In your markets, how do you expect target valuations to evolve in 2021 compared to 2020?



Pressure on pricing is largely the result of a narrowing of focus by sector, with many Covid blighted industries considered no go areas. Only 20% of buyout respondents showed no industry preference for 2021, down from 32% in 2020. Meanwhile, over half – 55% – are interested in pursuing IT assets, which have benefited from soaring demand due to remote working restrictions, up from 32% in 2020, while 54% are eyeing healthcare opportunities. Environmental services are also in vogue.

“Private equity firms are piling into a select group of ‘Covid winners’, which is inevitably having an impact on pricing,” says Colson. “That is putting a clear onus on GP discipline, in origination, but also on the ability to add value. Those with genuine industry insight are likely to successfully ride these sector tailwinds.”

STAYING CLOSE TO HOME

Interestingly, as well as reducing the number of industries they are actively investing in, GPs are now also more likely to stick to their domestic market. Only 59% plan to invest outside their home borders, down from 70%. This trend is particularly acute in the Nordics, Benelux and UK.

But despite the intensification of competition around a shrinking pool of assets, private equity firms remain bullish about the year ahead. Indeed, with 71% of GPs worried about mounting levels of dry powder – compared to 49% in 2020 – the industry is not going to be deterred by high prices. An overwhelming 85% believe 2021 will be a good year to deploy capital *(Exhibit 6)*, and 93% for managing their portfolio.

However, after a brief sales bonanza in late summer as the M&A market reopened, allowing GPs to dispose of their lowest hanging fruit, exits are likely to remain muted. Just a third of respondents view 2021 as a good market for realisations. There is also some uncertainty around prospects for fundraising over the next 12 months.

Two thirds of GPs believe that 2021 will be a good year for amassing capital, down only slightly from 72% a year earlier. But notably, only 43% expect to raise more than their previous vintage, down from 52%. Meanwhile, although the private equity allocations of pension funds and insurers are expected to continue to grow, it may not be with the same dynamism as previously. Critically, LPs are also increasingly scrutinising the question of returns vs stock markets, with 49% of GPs noting this trend.

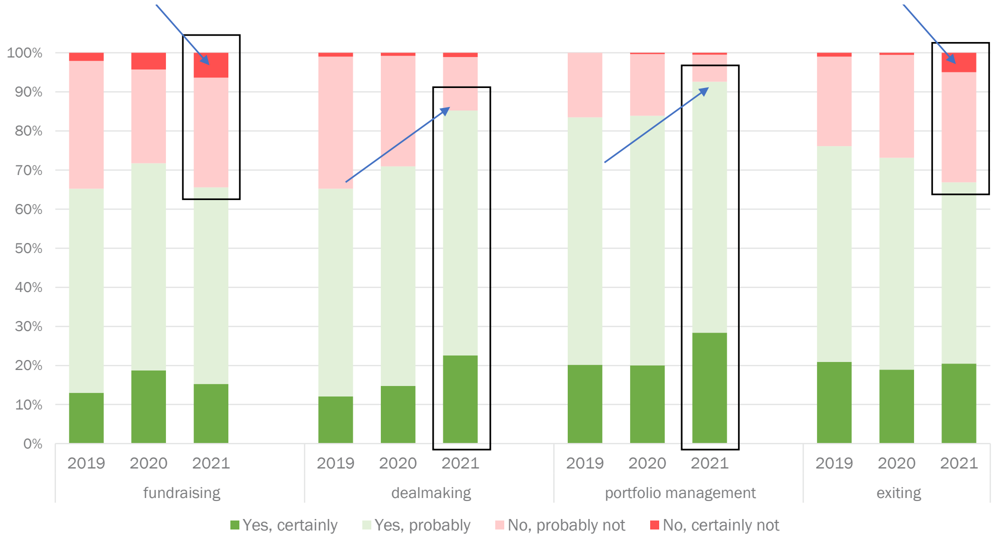
“Investors have poured more than $2trn into buyout funds over the past decade for the simple reason that they have outperformed the alternatives – namely the public markets. But a number of academic studies have recently cast doubt on that outperformance particularly for the period since the financial crisis. And stock markets bounced back to their pre-Covid levels quite quickly,” says Colson.

“There is a growing suggestion that private equity and public markets returns are converging on a net-of-fees basis,” Colson adds. “When you take the expected illiquidity premium into account too, that has to raise questions about future fundraising. In reality, of course, it will result in a flight to quality.”

EXHIBIT 6

A GREAT YEAR FOR CAPITAL DEPLOYMENT… BUT A CHALLENGING ONE FOR EXITS AND FUNDRAISING

Will next year be a good year for...



BEYOND RETURNS

Meanwhile, Covid is likely to have a transformational effect on private equity's approach to ESG *(Exhibit 7)*,. The pandemic has renewed focus on social concerns, whilst environmental challenges have not been allowed to fade from view. An overwhelming 82% of European GPs believe that private equity will raise its game in ESG as a result of the pandemic, with strong consensus in every region, size bracket and market segment. ESG was already an important focus for GPs in our last surveys; it has become a essential consideration. 63% of respondents now have ESG in their top priorities (up from 48% in 2020 and 36% in 2019) and 26% consider it their number 1 priority for 2021.

And, indeed, the industry is confident about the positive influence it already has particularly with regards to the energy transition, as well as health and education. It does acknowledge, however, that the asset class continues to fall short in some areas. Only 30% of respondents feel that private equity makes a positive contribution to issues around poverty and inequality, rising just slightly to 42% on matters of diversity representation.

> "THERE IS AN UNMISTAKEABLE SENSE THAT MANAGERS MUST INVEST FOR MORE THAN MERE FINANCIAL OUTCOMES"

Impact investing is nonetheless a major theme with 15% of responding managers already having launched an impact strategy. A further 18% expect to raise an impact fund in the next 12 to 24 months, with particular interest stemming from the Nordic region. This means, impressively, that a third of European GPs could become impact investors within the next two years.

We are also seeing a divergence away from the classic LBO deal, with 84% of GPs planning to explore more growth opportunities, including 79% of buyout specialists, irrespective of size of fund. In addition, European managers are demonstrably willing to innovate, with 42% planning to launch a new strategy this year – up from 30% in 2020.

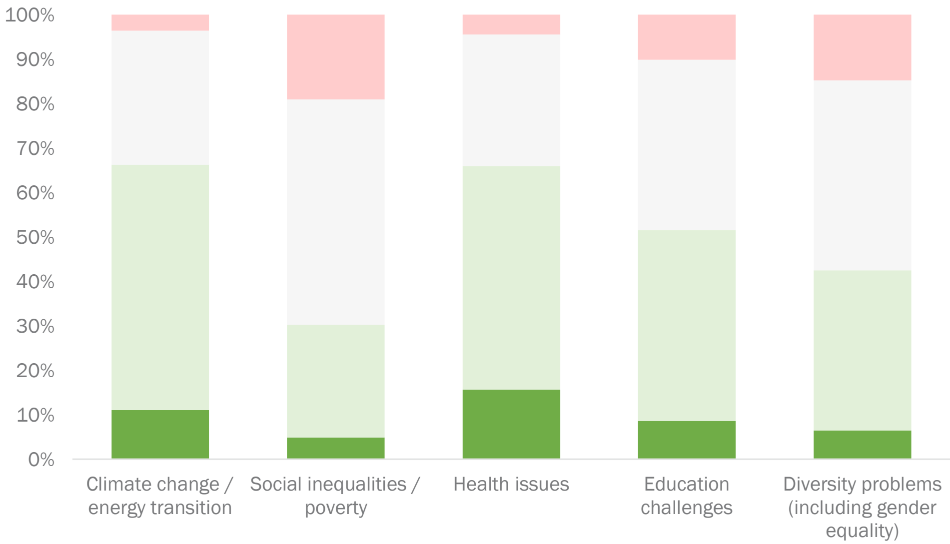
It is clear then, that Europe's GPs are not letting the small matter of a global pandemic thwart their ambition. Private equity firms have been quick to adapt to a new way of working and are now keen to exploit market dislocations to grow their portfolio companies, and their own franchises.

"Tellingly, however, and perhaps in contrast to the aftermath of the financial crisis, there is an unmistakeable sense that managers must invest for more than mere financial outcomes," Colson says. "In a shift that could prove vital for the sustainability of the asset class, private equity is embracing the opportunity to support the economic recovery, whilst also promoting the agenda for environmental and social reform."

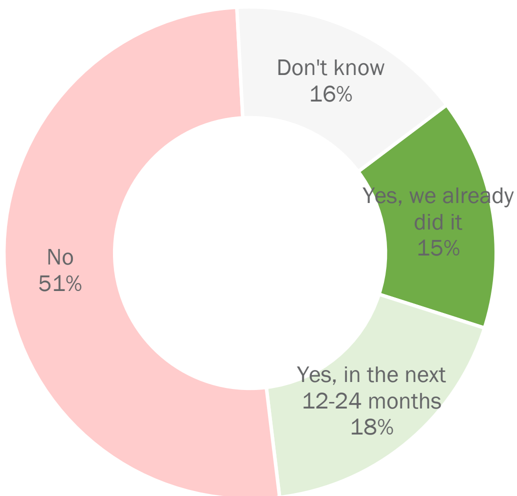
EXHIBIT 7

ESG IS PE TOP PRIORITY – WITH AN « S » EMERGENCY, AND A GROWING INTEREST FOR IMPACT STRATEGIES

What is the current contribution of PE to address...



Do you expect to launch an impact fund/strategy ?



SINCE 2019, NATIONAL PRIVATE EQUITY ASSOCIATIONS HAVE HELPED IPEM TO CONDUCT THIS PAN-EUROPEAN SURVEY. WE WOULD LIKE TO THANK THE 16 ASSOCIATIONS THAT PARTICIPATED IN THIS SURVEY AND HELPED IN ITS REALIZATION OF THE 3RD VINTAGE.

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