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Global Outlook
2022
PRIVATE EQUITY WIRE



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GAINING A COMPETITIVE EDGE THROUGH WEB TRAFFIC DATA AND INSIGHTS

Competition for deals in the realm of private equity continues to rise sharply. As investor demand soars and managers jostle for deals, new sources of information, such as web site traffic data, can provide an edge over their peers to help identify robust investment opportunities, improve due diligence processes and ultimately grow portfolio companies .

DUE DILIGENCE

By using web and app traffic data in conducting their due diligence, private equity managers can get a 360° view of company and sector health. This perspective is built using data from over 1 billion websites and more than four million apps.

"Since Similarweb collects data from such a breadth of websites and apps, managers can gain insights via a comprehensive view of a company and the industry in which it operates," outlines Lavery.

This data can also be used to fill gaps where, historically, little to no data has been available. "Similarweb has international data, so for global companies that do not provide a granular regional breakdown, we can provide a country-by-country performance view," Lavery says. Providing an example, he details: "Managers looking to launch a product or grow a business in a new market can examine the traffic there prior to launch. They can analyse, for example, the brand perception, and identify where the opportunities are ahead of making that move."

SOURCING INVESTMENT OPPORTUNITY

The notion of using website traffic data to locate investment opportunities can be taken even further. Lavery notes: "Managers can use digital behaviour data to enrich their insight and find signals in any company they are tracking."

Most PE managers have access to a number of data sources and this alternative dataset would provide them with a real time view of a company or sector. "Whereas they, historically, might have checked on a company once a year, now they can get a monthly view on how the company's trajectory is progressing and find inflections in that performance," Lavery highlights.

He observes how in using this data, some of the larger private equity firms are starting to operate in a similar way to quant funds; they are using high volume datasets to understand when is the right time to initiate a conversation and engage with a company to consider making a deal.

SUPPORTING GROWTH

Website traffic data is also highly valuable post-investment, to support PE managers in monitoring their portfolio companies and growing those businesses efficiently. "By leveraging this data, managers can improve a portfolio company's marketing strategy, drive traffic to its website and grow its business," Lavery explains.

Preeminent technology investors, Naspers, have exalted their use of Similarweb's data and use it as a key part of their dealmaking. The venture capital group relies on Similarweb to identify emerging players around the world and benchmark them as part of its due diligence process. The data also enhances the performance of its portfolio clients with valuable market insights.

To learn more about Similarweb visit www.similarweb.com/corp/investors/



ED LAVERY
DIRECTOR OF THE INVESTORS SOLUTION

Ed heads SimilarWeb's Global Investor Solutions business. Ed joined SimilarWeb four years ago and has been spearheading the solution to help investors integrate Digital Alternative Data into their investment research. He has also worked with many of the world's leading brands, shaping their digital strategies through market intelligence data. Prior to SimilarWeb, Ed started his career in Investment Banking in London, working at Rothschild and DC Advisory.

A HOLISTIC APPROACH KEY TO EFFECTIVE TECHNOLOGY DEPLOYMENT

Technology has had a deep-seated impact on the way private equity investment operates. But as macro tech forces move at pace, PE firms should approach business technology in a holistic manner and focus on solutions related to cloud, risk and digital experience.

The main areas PE firms should, at least, be aware of are digital experience, cloud, risk, business technology, core modernisation, digital reality, cognitive and blockchain. And although momentum is building in each of these, George Ralph, Global Managing Director and CRO of, RFA believes some are worthy of greater attention as PE firms start to enhance their digital offering.

"We provide business IT solutions to work with clients to advance their overall business technology offering. I would suggest the key focus here should be on cloud, risk and digital experience. All are interlinked and if approached as a whole, can enhance security, efficiency, reporting, decision making and client experience," he outlines, "The important thing is to understand and set up the right framework. This helps simplify the choices a firm needs to make but also decide whether to outsource your business IT or not. It would also assist managers in understanding what their macro tech looks like, which is vital when dealing with the regulator."

DRIVING BUSINESS GROWTH

PE firms are having to wrestle with a number of different pressures and Ralph notes that astute managers recognise the interoperability between macro technologies: "Properly framed, the infrastructure question we should all be asking is about how we can drive business growth and create long term scalable solutions. The results are enterprise success, greater efficiency and productivity, reduced cost, and better risk mitigation."

He once again emphasises the importance of a holistic approach: "If cloud, risk and modernisation are seen as an organic whole rather than as separate challenges, a firm is able to build or invest in a more scalable and flexible business IT solution. This improvement is vital as investors and regulators demand more immediate action from companies to address various issues that require additional data strategy and reporting like environmental, social and governance issues."

Ultimately, firms will need to be prepared to take action and evidence they are taking to make changes, so they are able to support investor and due diligence requirements and keep pace with their competition.

The speed of change in the technology space can be considered one of the most significant challenges PE managers face in trying to harness the full benefits it has to offer. This is why, Ralph stresses the importance of having a business IT partner: "Managers need to remain focused on their own business growth, not the infrastructure behind it. The upheaval of our working practices over the last couple of years has really helped with advancing technology ideas to the PE market at a faster pace than we would have seen had we remained in a traditional working model.

"We aren't there yet, but macro tech includes digital reality and cognitive activity; this kind of experience could completely change the way managers interact with investors. We aren't in the metaverse yet, but I am a firm believer that the way managers and investors do business will change in the medium term. This will of course happen in every part of our life, not just transactional business."



GEORGE RALPH
GLOBAL MANAGING DIRECTOR & CRO

As Global Managing Director of RFA, George is a technology and business leader with a proven track record of strategic alignment, process improvement and guidance. Having been both a COO and a CTO of his own technology firms over a nineteen-year period, he looks to provide transparent guidance to every business he serves and the people he leads. George has extensive delivery and technical experience in network and server architecture, large-scale migrations utilising leading technology brands, and IaaS offerings.

RED HOT COMPETITION AS DEMAND PERSISTS



Despite two years of uncertainty brought about by the pandemic, a few things have remained relatively constant: a low interest rate environment; bouyant demand for private assets; and intense fundraising activity. During 2021, the latter moved to a record high.

The private equity market – in terms of AUM and number of private equity investors – has tripled in size over the last decade.

There are no signs – yet – of this growth halting in 2022.

Fund managers have been quick to ride recent waves of investor interest in healthcare and technology-focused fund strategies, accelerated by economic lockdowns, but competition among these GPs for capital flows, assets and talent is now red hot.

Prudent managers see a tipping point this year in areas such as ESG and alternative data where competitive advantage can be found. Others are doubling down on increased specialisation, platform extensions and regional expansion.

Private equity will no doubt continue to be a highly sought-after asset class by the end of this year, but much of its future growth is expected to come from emerging areas, such as growth equity and impact investment.

How this growth plays out will be determined by the greatest trend currently shaping the private equity fundraising market: the dominance of established mega-funds.

Average fund size continues to rise and the pace of new funds entering the market is accelerating, but the number of funds closing is down from its peak in 2017. For LPs, it is a busy and crowded market, and many do not have the time or resources to consider allocations to new or first-time managers.

Will this limit innovation or have other unforeseen consequences in the long-term?

High deployment rates suggests that dry powder is not a problem but the middle market and some of the newer sector specialists will have to demonstrate even stronger returns to compete with larger managers returning to market. The race continues.

Private Equity Wire would like to thank everyone who contributed their valuable insights to this year's report.

Colin Leopold
Head of Research & Insight
Global Fund Media

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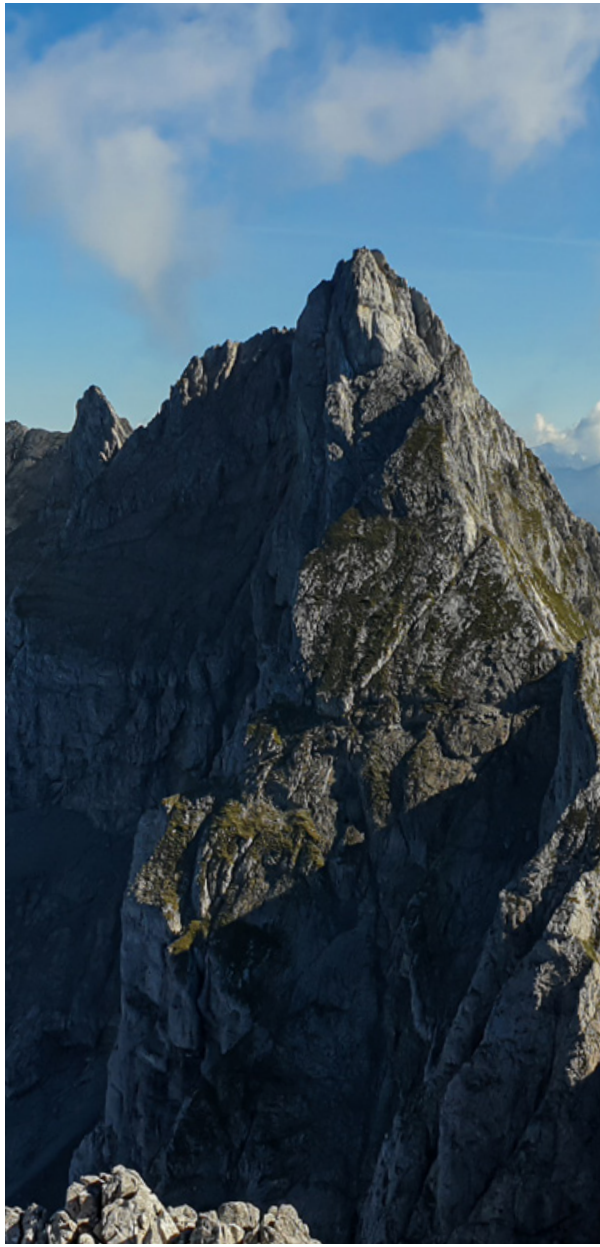
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CHAPTER ONE

MACRO



"2022 IS LIKELY TO BE A TIPPING POINT, AND WE BELIEVE THE ABILITY TO LEVERAGE ALTERNATIVE DATA WILL SEPARATE GOOD FROM GREAT PRIVATE EQUITY PROVIDERS"



RUSSELL STEENBERG

GLOBAL HEAD, BLACKROCK PRIVATE EQUITY PARTNERS

In 2022, we look for continued performance supported by a low rate borrowing environment, open capital markets, pent up demand and dry powder, after two years of strong fundraising.

The size of the private equity market – in terms of AUM and number of private equity investors – has tripled in the last decade, as interest in the asset class increased and access was democratised. Investment and exit activity reached record levels in 2021; increased realisations fuel fundraising, and as a result, we are witnessing a shorter fundraising cycle. Despite such unprecedented growth on all fronts, we see little evidence for short-term slowdown and expect the current pace of investment to continue in 2022.

We are approaching the 2022 investment landscape with prudence.

Valuations remain high, which means selectivity will be as important as ever. GPs should look carefully at leverage ratios and how companies manage cash flow and liquidity through periods of market volatility. It is important to recognise where we find ourselves in an industry cycle, thinking about the past and also understanding future growth trends for a particular industry. At BlackRock, we remained focused on building diverse portfolios of high-quality businesses with defensible positions in markets with growth opportunities.

Competition for investments heightens the importance of broad sourcing networks, industry sector expertise and operational skills. In North America, price discipline will be key as purchase price and leverage multiples near record levels. Europe is likely to follow a similar trajectory, with elevated valuations and investment appetite, albeit with dispersion across the region. In Asia, there is elevated short-term risk given geopolitical tensions and increased regulation that may limit potential exit options for deals in China; however, we believe China continues to offer strong long-term opportunities in technology, healthcare and consumer goods. We have a positive outlook for other regions in Asia, particularly buyout and growth opportunities in South Korea, Australia and Japan.

Alternative data presents the potential to revolutionise private equity investing, provided investors are able to harness, analyse and turn takeaways into actionable investment decisions. Since private companies by their nature lack public filings, sources of alternative data – news outlets, broker reports, internet blogs, search trends, satellite imagine, and beyond – become particularly appealing in the exponentially larger private market investment universe.

2022 is likely to be a tipping point, and we believe the ability to leverage alternative data will separate good from great PE providers in the next few years. GPs will have to go beyond data gathering; the true advantage will lie in the ability to discern the ways in which the data points can be used to identify likely outperformers and make smarter investment decisions. We see alternative data as an enhancer of the fundamental investment process which can provide managers with an information advantage.

We believe the increased attention to ESG in private equity will continue in 2022. Private equity is well positioned to play a leading role in the transition to a sustainable economy given its long-term focus, direct governance and additionality. While climate-related investments may seem the largest opportunity set, we remain optimistic about opportunities in advancing good health and wellbeing, as well as education and financial inclusion.

"SUCCESS IN 2022 WILL BE DETERMINED BY A HIGH LEVEL OF SELECTIVITY AND A FOCUS ON THE COMPLEXITY PREMIUM"



NILS RODE

CHIEF INVESTMENT OFFICER, SCHRODERS CAPITAL

Fuelled by Covid-induced monetary and fiscal stimulus, as well as strong past performance, interest in private equity has been rising sharply. We expect this to continue in 2022.

This has brought fundraising levels in some areas significantly above their long-term trend. Typically, such a situation can put pressure on vintage year performance expectations. We therefore believe that the illiquidity premium is under pressure, while other drivers of outperformance – such as the complexity and size/smaller investment premia – remain intact.

Furthermore, in terms of private equity fundraising, the US and Europe have been notably above their long-term trend, especially for venture and growth capital. Over the past five years, venture and growth capital fund raising has grown by 240 per cent, driven by the emergence and growth of the so-called unicorns (privately held companies with valuations above USD1 billion). In contrast, annual buyout fundraising in the US and Europe increased by only 59 per cent in the same period.

In such an environment, our view for 2022 is that – besides adherence to a long-term strategy and investment discipline – the main determinants of success within private equity will be, a high level of selectivity and a focus on the complexity premium. The complexity premium can be captured in private equity when two factors meet. Firstly, when a situation arises that is particularly complex in terms of access, risks and opportunity. Secondly, when rare skills are deployed to source, select and negotiate, develop and exit the investment.

On a sector-by-sector basis, we continue to see healthcare, technology and consumer as the three most interesting sectors within buyouts. Even though competition for such deals has further increased given the boost the pandemic has given to these sectors, we continue to see attractively priced opportunities in the small and mid-sized segment of the market.

We also observe that strong alignment of investments with the UN's Sustainable Development Goals contributes positively to investment performance, especially where highly active private equity managers make transformational improvements to companies.

With regards to secondaries, we view the most interesting opportunities within GP-led transactions. These allow fund managers to keep and develop some of their most attractive portfolio companies for a longer time period than they would otherwise be able to do. This is the fastest growing part of the secondaries market. It is expected to generate USD60 billion-plus of secondary deal volume in 2021, up considerably from prior years. GP-led secondaries are typically highly complex transactions, involving many different stakeholders, and this creates an advantage for those investors who are already a primary or co-investor in those assets.

Moving onto venture capital, the last 12 months have seen an extraordinarily positive environment globally, both for follow-on financing and for exits, especially for IPOs. However, increasing fundraising and dry powder are a concern, particularly for late stage and pre-IPO financings of high growth companies where we are seeing valuations significantly above historical metrics. We favour the seed and early-stage part of the market and see more opportunities here to capture the complexity premium compared to later stages. The most attractive opportunities in new and emerging themes are across technology, healthcare, and climate tech.

One emerging theme in technology is 'the future of work' as many companies will have a permanent hybrid work environment with office-based and remote teams. Within healthcare, we are exploring companies focused on drug discovery platforms with potential break-through therapies in solid tumours, cardiovascular, and organ regeneration. Climate tech is one the new emerging themes focused on technologies that reduce CO2 emissions.

Overall, the results of our recent Institutional Investor Study found that private equity was the stand-out asset class within private assets, in terms of investor demand. We expect the popularity of private equity to remain strong next year as we anticipate it will continue to deliver robust performance and returns for our clients.

"THE TRILLION-DOLLAR QUESTION FOR PRIVATE EQUITY NOW IS 'IS THERE A CEILING ON THE MARKET?' AND IF SO 'WHERE IS THAT?"



PETER WITTE

ASSOCIATE DIRECTOR, PRIVATE EQUITY, EY

The trillion-dollar question for private equity now is 'is there a ceiling on the market?' and if so 'where is that?'.

The overarching 40,000-foot view is that we're in the middle of this transformation in terms of how companies get funded. I think that mainstream, traditional buyouts in the US and Europe will continue, but a lot of the new growth for the industry is going to occur in new deals and new strategies. You see this with the focus on growth capital and funds which are out there raising these huge growth capital funds. It's been an area in which private equity has dabbled for most of its history, but GPs haven't raised this kind of money before, and they haven't been so involved in the growth capital. So some of these new strategies are really going to drive a lot of growth.

Also, when we think about what private equity would have looked like even five years ago, a lot of the firms – not all of them, but many of them – were organised around sectors and sector teams. A private equity fund was a collection of all these different sector verticals. Now you're seeing a bifurcation of that. Where, if you're a large firm, you can use your scale, and pursue a thematic approach: so it's logistics, it's data infrastructure, it's retail, it's all of these sort of cross-sector themes. If you're a smaller firm, you're still taking your sector approach, and maybe you're making it a sub-sector approach: so you're not focused on healthcare anymore, you're focused on healthcare IT. There are still generalist, middle market firms out there but it's getting harder and harder to do. This segmentation of different strategies is also driven by the LPs looking to dial up their exposures a bit more.

Where will this go in 2022? Software has just been a massive theme. It fluctuates from maybe a quarter to a third of total private equity investment activity. And so, there's a question of 'how long does that have to run'? Has that investment theme gotten too crowded, or are we still in the very early stages of where that's going to go? Opinions are really all across the board; you have LPs that are worried about the amount of exposure they have in the tech space; and you have LPs saying 'This is the thing that's going to play out over the next 30, 40, 50 years'. That seems to be the prevailing view. The market is looking at not just pure play software, but now really using software as sort of a lever for value creation.

ESG is the other theme we will see more of in 2022. The number of conversations that we're having with firms around ESG-related issues over the last 18 months has absolutely exploded, it's gone from being on the backburner to something that's really front and centre. You see it in the hiring that they're doing, elevating these mid-level roles, or bringing in very senior people that report to the CEO. Firms are realising that this is another value creation level. If they invest in making a company better along some of these non-financial measures, then that will translate into better returns for their investors as well.

But both of these themes play into a question around talent. Digital and ESG are really new capabilities for a lot of these private equity firms. Firms are now making huge investments in data science, above and beyond the traditional deal team, operations partners, and back office. How do you source those people? How do you integrate them into the firm, in terms of their compensation and in terms of culture.

And how do you do that in a way that's as inclusive as possible, and that leverages the benefits of a diverse workforce?

"WE ARE IN A SUPER-CYCLE, BUT WE ANTICIPATE THIS WILL SLOW DOWN AT SOME POINT. LET'S BE PREPARED NOT TO ALWAYS GO IN ONE DIRECTION"



MARKUS BENZLER

GLOBAL HEAD MULTI-MANAGER PRIVATE EQUITY, UBS REAL ESTATE & PRIVATE MARKETS

This year was great for the private equity market.

Since Covid-19 dipped the market in Q1 2020 it has been a strong run, and actually even on a longer perspective, since the global financial crisis, private markets have enjoyed consistent and strong returns, with a few exceptions here and there.

In general it seems to be like a super-cycle, although we anticipate this will slow down at some point for a number of reasons.

I think in 2022 there will continue to be spill-over effects from public markets. I don't know if it's everybody's view, but the common perception for public markets is that there's more volatility [to come] and also opportunities, but more of a sideways movement than up or down.

[The shock for private equity investors in 2022] could be just related to the real economy, or it could be political or based on other movements affecting stock exchanges globally. I think it's very likely that something like this will happen in 2022 and this will impact private market valuations. It will be with a lower correlation than one but it will affect private markets. We wouldn't go so far as to say 'prepare for it' but we are very mindful that this can happen and quite frankly I am not sure, especially on the limited partnership side, how prepared people are for that.

On the GP front, if they are managing buyout funds and they're more linked to the industrial sector or invested in retail companies, they've typically already worked hard in the last one and a half years due to the real economic impacts of Covid-19. Obviously some GPs are less prepared than others but I think on the GP side, they're quite well equipped in terms of what to do if the environment changes, especially among those that have been around for longer than others and have the skill set to weather the storm, whatever might come.

We have a much more cautious stance towards our own investors, but also to our management. Let's be prepared not to always go in one direction. In the best case scenario, such a change will come from a political angle or from stock markets, with less of a root in the real economy, but it could also arise from recent developments with Covid-19 which is continuing to impact markets, even with a vaccine.

CHAPTER TWO

FUNDRAISING



"LPS ARE STAYING THE COURSE ON THEIR PACING PLANS – INCREASING THEIR ALLOCATIONS IN SOME CASES – AND WE FORESEE ANOTHER ROBUST YEAR FOR FUNDRAISING IN 2022"



LINDSAY CREEDON

PARTNER, STEPSTONE GROUP

Following the shock and dislocation of the pandemic, private equity fundraising in 2021 fully recovered back to its 2019 levels. The average fund size continues to rise, and the velocity of new funds entering the market is accelerating. At the same time, LPs are staying the course on their pacing plans – increasing their allocations in some cases – a clear sign that investor interest in this asset class remains strong. As the economy continues to show signs of recovery and growth, we foresee another robust year for fundraising in 2022.

With more exit paths available, including SPACs and continuation funds, realisations have increased, and LPs continue to seek opportunities with an attractive risk-return profile in which to deploy capital. As such, fundraising cycles are shortening. In 2021, we saw the average time for GPs returning to market fall to approximately three years, compared with a four-year gap historically. Fund sizes are growing too, especially as small and mid-market funds graduate upward to larger transactions.

As a result, the fundraising market is crowded. From an LP perspective, re-ups are coming around quicker than ever, leaving less capital available for emerging managers to be included in mature programs. Many LPs have small teams devoted to private equity and therefore limited capacity to vet new managers. They are also incentivised to stick with the highest performing GPs currently in their portfolio. On the flip side, top-tier GPs are spoilt for choice when it comes to managing their LP base, tapping existing relationships for increased allocations.

With a faster pace of fundraising and deployment, what of due diligence? The pandemic forced GPs and LPs to adapt to a virtual due diligence environment, though in-person meetings did slowly return in the second half of 2021. But the lack of in-person meetings over the last two years has hurt managers coming to market for the first time, with the exception of new managers with demonstrable track records from prior firms.

Another trend we're seeing is the creation of more funds and products targeting different parts of the market. For example, a manager with a successful late-stage growth equity fund may tap existing LPs to create a fund to target early or mid-stage growth opportunities. Similarly, we expect more impact funds to come to market in 2022, by both small firms dedicated to impact investing, and large institutions leveraging the resources of their firms to create them. Along those lines, ESG principles have been more fully incorporated into investment underwriting by LPs and GPs alike.

The trend toward specialisation will continue, as sectors like tech and health care continue to penetrate more of our everyday lives. GPs with strong sector specialisation have shown higher returns than generalist managers and have had an easier time raising new funds. But even for industries that have fallen out of favor, all is not lost: savvy private equity investors continue to emphasize the importance of diversification by sector, strategy, geography and vintage year. In addition, with the growing volume in the secondaries market, expected to be USD100 billion in 2021, it is easier for investors to achieve such diversification and allocate incremental capital to sponsor-backed companies.

All of the above gives 2022 a strong fundraising floor, and we look forward to a healthy market in the coming year.

"THE FUNDRAISING CRUSH IN 2022 WILL INEVITABLY SPILL OVER INTO 2023 AS DOING EUR300 BILLION IN ONE YEAR IS NOT POSSIBLE"



ANDREW BENTLEY

PARTNER, CAMPBELL LUTYENS

2022 looks like it will be a very congested year for private equity funds, with potentially twice as much capital being sought from LPs than the busiest year we've ever seen.

Plenty of GPs will get funded very fast, but many GPs will have a more drawn-out process as LPs figure out what allocations they will get into rival GPs funds before deciding what is left for the rest. This is despite most GPs having had very good performance in the last 12 months.

The crush in 2022 will inevitably spill over into 2023 because the industry won't be able to raise the EUR 300 billion that the GPs are asking for during one single year. It's not possible.

We've already seen a bifurcation of outcomes in fundraises: some get done very quickly, by which I mean, within four to six months; and others take 12 to 18, or even 24 months.

For a few years now, the bigger, established funds have been coming back with larger funds quicker. It creates congestion and a lot of pressure. And that pressure gets dissipated in different ways.

We've also got private wealth making inroads into the sector. In general, private wealth feeders focus mostly on the biggest brand name GPs and don't seek the middle market firms. All these trends support the bigger firms.

So where are we going to be at the end of 2022 if that continues? The middle market and the independents and sector specialists are going to need to generate even stronger returns to be able to compete.

The big GPs have been building their sales teams and proliferating their product offerings trying to dominate the LP capital available. It's an unbelievable power play out there, with these groups trying to get as much LP allocation as possible by addressing every single part of an LP's private fund requirement.

High deployment rates suggests that dry powder is not a problem. The speed of deployment is a symptom of the fundamental shift in the upper reaches of the industry from focusing on carried interest from investments to seeking to maximise the value of the shares in the GP itself. Deployment drives fund growth which drives share prices and shareholder value. GPs are of course concerned about entry values, but there's not fundamentally much most of them can do because they have to keep deploying, and we are in the market that we're in.

Specialism is how the middle market in particular is trying to manage this: focusing on sectors and themes where they have a clear edge. That edge is necessary and a very real reason why they and not the other 15 to 20 people bidding for an asset will secure it. So generalist private equity is out and having a specialist focus is in. In 2021, specialisms in technology and healthcare were very sought after and in 2022 we expect specialisms in sustainability and energy transition to be very sought after.

"GROWTH FUNDS ARE BECOMING THE 'MUST HAVE' PRODUCT EXTENSION FOR VENTURE CAPITAL FUNDS"



THOMAS MCCOMB

PRIVATE EQUITY PORTFOLIO MANAGER, JP MORGAN ASSET MANAGEMENT

We expect to see robust activity in the private equity fundraising market in 2022, similar to what we have seen over the past several years.

There are two main factors driving this. Firstly, returns continue to be strong. Buyout returns have been compelling, especially in growth segments such as technology in recent years. Additionally, after a difficult decade in the 2000s, returns in venture capital (VC) and growth funds among the best firms have done an exceptional job of securing more capital to each of the sectors and attracting new entrants. Returns on well-implemented private equity portfolios have produced a substantial premium on the public equity benchmarks.

Secondly, distributions have been quite strong, both from buyout and VC and growth funds – we have seen a robust exit market. Trade and financial buyers have both been quite active. We have also continued to see a robust IPO market, with some firms using SPACs as another avenue to a public exit. We would expect the years following 2022 to continue to be favourable for private equity funds raising, assuming the current conditions with regards to returns and distributions persist.

Established investment firms continue to use their franchises to generate product extensions. While this has been common among the 'mega-funds' for a number of years, we are starting to see funds in the small and mid-markets pursue such strategies. We are seeing larger and mid-market firms raise small cap funds, co-investment funds and credit funds. Growth funds are becoming the 'must have' product extension for VC funds, with others considering additional verticals and geographies.

In 2022, firms with strong established track records, with differentiated strategies, should continue to perform well.

Technology is playing a role in a few ways here.

Firstly, the rise of virtual meetings particularly by VC firms, which were being implemented before the pandemic, have accelerated. While we do not expect in-person meetings to be eliminated, many initial due diligence meetings and some follow up ones are now conducted virtually. These enable GPs to spend more time in their office raising capital in place of extended road shows. Secondly, technology also enables much more sophisticated use of data which helps GPs better articulate their story, and LPs to better evaluate them. Finally, technology as an investment sector, is obviously a core area for focus for VC and growth firms. It continues to grow in importance for many buyout firms.

In terms of new talent, a number of investors, particularly newer ones to private equity, have established emerging manager progammes where they invest in funds raised by firms they expect to be the established firms of the future.

Newer groups will likely face competition from industry incumbents in two ways: the aforementioned product extensions by established firms; and an increased velocity of capital investment. Many firms are seeing a more rapid investment pace in this cycle which is necessitating a return to raise new funds more quickly than originally anticipated. In some cases, three to five year investment periods have shrunk to one and a half to three years.

In addition to having strong investment track records, new private equity firms will need to differentiate themselves through their strategies to overcome such challenges. Co-investments remain in high demand as do stapled secondaries. Investors want the ability to invest capital with more visibility, lower overall fees, and reduce blind pool risk.

"MORE US-BASED VENTURE FIRMS WILL EXPAND THEIR PHYSICAL PRESENCE IN FRONTIER MARKETS, ESPECIALLY LATIN AMERICA AND THE MIDDLE EAST"



CHRISTINE TSAI

CEO, FOUNDING PARTNER, 500 GLOBAL

We believe that private equity and venture capital (VC) fundraising will be as active – if not more so – in 2022 as it was in 2021.

Last year's VC fundraising activity through Q3 alone surpassed 2020's record, and is expected to break the USD100 billion mark by the end of 2021. As pension funds, endowments, sovereign wealth funds, universities, and high net worth individuals continue to seek increased exposure to private markets, we think the influx of capital into private equity and VC funds will continue at an accelerated pace.

Looking ahead, there are several global technology trends that we expect VCs will be watching closely. We believe an increasing number of firms will seek opportunities to invest in companies that are based outside of traditional tech hubs, both within and outside of the US, which also means investing in less obvious founders who come from various geographies, demographics, and backgrounds.

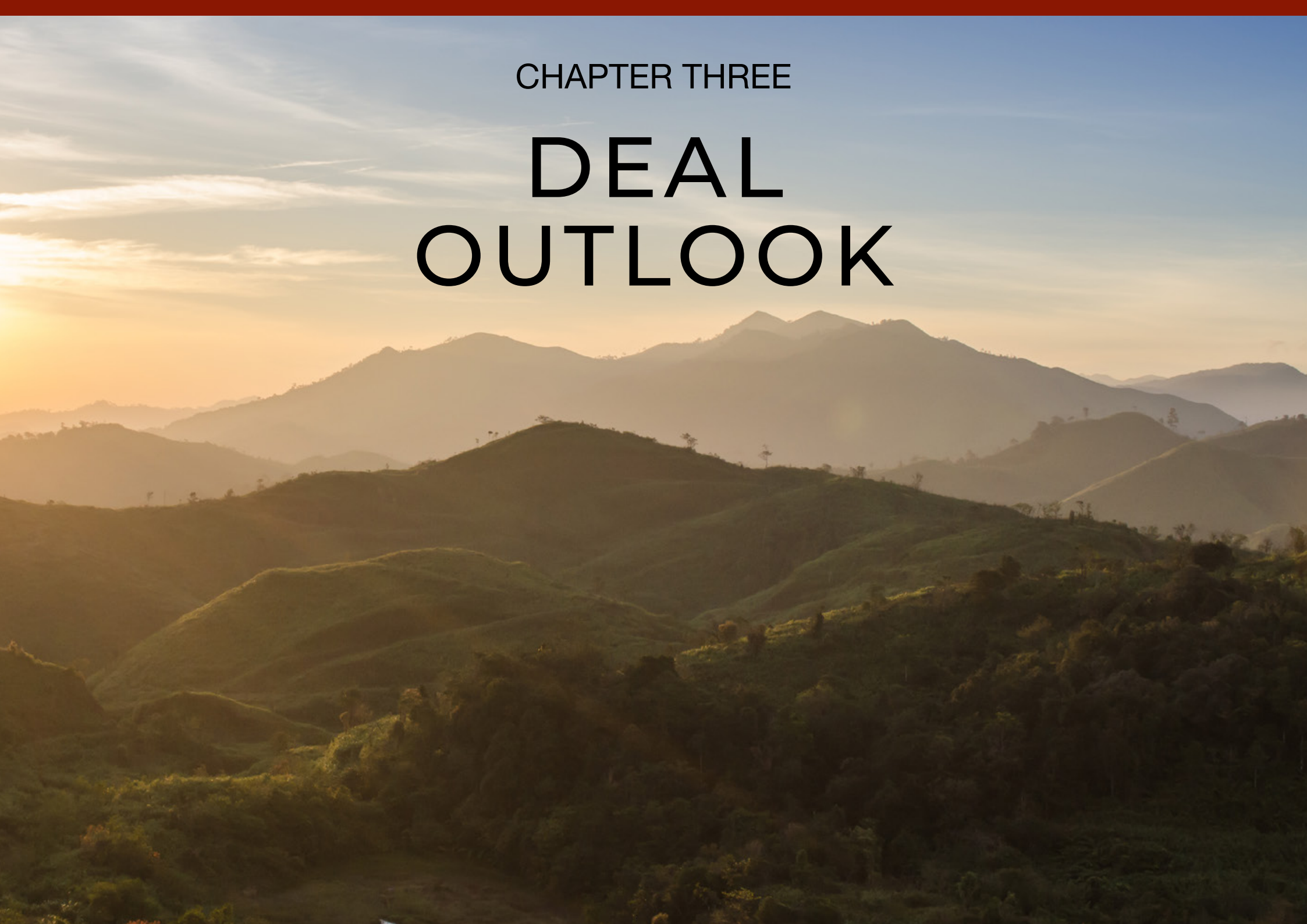
As a result, we will potentially see more US-based venture firms expand their physical presence in frontier markets, especially in Latin America and the Middle East. We believe firms that focus their time and attention on building strong relationships in nascent tech ecosystems are the ones that are likely to be most successful long-term.

We also believe that the momentum we saw in 2021 will likely carry over into 2022. Right now, deal activity is at an all-time high. Just in October, more than USD54 billion was invested in 2,000-plus companies globally. We're seeing accelerated growth in the fintech industry. Venture capitalists invested a record total of USD39 billion in the first three quarters of 2021 in fintech companies. This already surpasses the USD20 billion raised for all of 2020.

While macroeconomic issues cast a shadow on the economy, we believe tech investing will continue to grow post-pandemic. We are backing entrepreneurs who are building innovative solutions to meet evolving consumer and business needs.

The world is still combating a global pandemic, which continues to pose a risk to populations and businesses in certain sectors, such as travel and hospitality, retail, supply chain and logistics, and more. There are social and economic challenges that investors and founders need to be ready to navigate in the year ahead. Inflation, which soared to a 40-year high in early December, is of concern, as bottlenecks in the supply chain remain an issue.

We are adapting our investment framework to reflect the way some industries that benefited from the pandemic initially now need to adjust given the recovery, and how others that saw activity grind to a halt are seeing signs of life. Despite challenges, we believe there are opportunities for a new generation of disruptive companies worldwide, as the pandemic accelerates digital adoption and a new era of innovation unfolds.



CHAPTER THREE

DEAL OUTLOOK

"WITH THE BROADER GLOBAL RECOVERY, INDUSTRIALS AND CONSUMER ARE STARTING TO SPRING BACK AND ACTIVITY ACROSS SECTORS IS GRADUALLY BALANCING OUT"



CRAIG MACDONALD

MANAGING DIRECTOR, HARBOURVEST

2021 was a year of considerable activity, particularly in the tech and healthcare sectors, as investors sought resilient assets which were well-placed to weather, and even grow in, the pandemic environment.

However, in line with the broader global recovery, other sectors such as industrials and consumer are starting to spring back, and activity across sectors is gradually balancing out.

We have seen a meaningful increase in consumer deal flow, with growth in consumer discretionary being particularly strong. For example, consumer discretionary deal flow is up around 70 per cent in absolute terms in 2021 compared to 2020, and consumer staple deal flow is up 50 per cent in absolute terms over the same period.

We continue to see growth across consumer in 2022, but consumer discretionary is growing slightly faster than consumer staples. We think this reflects sentiment that while the pandemic remains, consumers and the wider economy are learning to live with it.

As we move out of the pandemic, it will be important to build a diverse portfolio which is protected against downside risk, while also being able to capitalise on opportunities as the economy recovers across all sectors.

The American economist Harry Markowitz once said: "Diversification is the only free lunch in investing." Private equity's approach to diversification has been in evidence ever since the global financial crisis (GFC). Pre-pandemic, the trend towards increasing exposure to technology and healthcare was already apparent. This was then accelerated further by the pandemic, as both sectors were positioned to benefit from changes in trends such as remote work. However, the increase in exposure is modest within funds which are meant to be sector agnostic.

It is worth noting that tech and growth-focused funds have increased in number and size, and many cross-sector managers have been able to increase their exposure to growth by providing LPs and prospects with tech-focused funds.

Despite the general trend of recovery, companies will still face challenges in 2022, particularly around inflation and supply chains.

Private equity as an ownership model is well placed to handle inflationary pressures, but we need to keep a careful eye on the pricing environment. Supply chain issues are also prevalent, especially given the pace and scale of recent disruptions – resolving these will be a key priority for the year ahead.

Looking ahead, investors will need to be particularly focused on their partnerships. For GPs, this will be crucial. Industry expertise and moving to address these challenges quickly will be a competitive advantage.

Superior managers' abilities to differentiate themselves from both public and private benchmarks against the backdrop of a potential downturn in markets is key and investors will want to be as selective as possible in their GP relationships. This has always been the case but will gain renewed focus as we move into 2022.

"A LOW SUPPLY OF SIZEABLE, HIGH QUALITY INDUSTRIAL PLATFORMS WILL CONTINUE TO DRIVE VALUATION LEVELS THIS YEAR"



NICK SEALY

CO-HEAD OF EUROPEAN INVESTMENT BANKING, BAIRD

There was a normalisation in industrial M&A in the third quarter of last year. It represented a 28 per cent share of European private equity activity, up from 20 per cent in H1 2021 for the middle-market (deal values of EUR100m – EUR500m).

However, this industrial M&A activity was skewed towards more defensive or growth sub-sectors such as packaging and automation. Industrial, much like other sectors, is experiencing significant bifurcation in terms of buyer demand and valuation between faster growing resilient assets that benefit from megatrends, such as ESG and digitisation, relative to those that do not.

The unprecedented nature of the current crisis with supply chain issues and high inflation is having a material operational and financial impact on most industrial businesses, a situation that is expected to continue until mid-2022. Some companies are able to pass on cost inflation to their customers contractually or otherwise, while others are struggling to agree price rises with their large original equipment manufacturer (OEM) customers. As a result, a number of sale processes that have yet to launch are being delayed to 2022, while some late-stage M&A processes are slowing as potential buyers refocus their due diligence to understand the impact of this current crisis on the target company.

In terms of a broader range of sub-sectors, we expect companies to come for sale in 2022, including those recovering from the impact of Covid, such as commercial construction.

Industrial assets vary in quality and size, and there will remain a scarcity of sizeable and high-quality targets relative to M&A demand, for example above EUR25m EBITDA and with an EBITDA margin above 20 per cent.

European buyout firms with record levels of dry powder have been winning competitive industrial M&A auctions, taking share from strategic buyers in recent years. The combination of high M&A demand and low supply of sizeable high quality industrial platforms increased valuation levels for top quartile assets in 2021; a trend we expect will continue in 2022.

US industrial corporates are strong acquirors of European targets, benefitting from valuation arbitrage (driven by elevated US public company valuations) and synergies. Industrial corporates are using M&A to reduce cyclicality, add technology and increase exposure to secular growth themes. In view of this, private equity firms will therefore face fierce competition for best-in-class assets, such as those with recurring revenue, connected products, ESG driven business models and automation driven demand.

Private equity's competitive advantage has been upfront work, researching the specific sub-sector and meeting management teams of European industrial targets before the launch of a sale process, to then move quickly and efficiently through due diligence and M&A negotiations. This dynamic will only become more important in 2022 as potential buyers determine which industrial targets they will invest both the time and the money needed to seriously pursue those opportunities.



"VALUATIONS NOW TEND TO BE HIGHER IN TECH AND HEALTHCARE BUT THEY ARE JUSTIFIED BY STRONG CONVICTION IN THE GROWTH OUTLOOK"

STEPHAN SCHÄLI

CHIEF INVESTMENT OFFICER, PARTNERS GROUP

With extremely short processes and high valuations having become the norm, the only way to prudently invest in this environment is to adopt a targeted sourcing approach, building strong conviction in those investment themes that will continue to generate sustainable growth, regardless of economic dynamics.

We pursue 40-60 investment themes at any given point in time across our four private equity sector verticals: technology, goods and products, health and life, and services. Many of the transformative trends reshaping the way we operate lie at the heart of our thematic investing approach and were accelerated by the pandemic.

One of these, the food value chain – from inputs to production and then to processing, retail and delivery – represents a significant opportunity set, with a similar market size to global pharmaceuticals. We have regarded this as a strategically critical sector for several years – something that has been highlighted by the Covid-19 pandemic. We believe the industry is now poised for sustainable long-term growth.

This is supported by three secular trends. First, the sector is shifting towards responsible and sustainable food production, with an emphasis on minimising the impact that agriculture has on climate change, increasing the share of organic agriculture and reducing food waste. Unilever, for example, has revealed that its sustainable living brands are growing 69 per cent faster than the rest of the business. Second, ensuring food security for the global population has become a key priority, with end-to-end transparency and traceability now expected to become the norm. Finally, modern consumers are shifting towards healthy consumption alternatives and are willing to pay a premium for sustainably and responsibly sourced inputs.

One particular sub-segment where we expect to find opportunities is the burgeoning alternative protein production sector. Meat industry leaders such as Cargill and Tyson Foods have already shifted operations and investments towards plant-based substitutes and cell-cultured products. The acceleration of plant-based foods, driven by health, animal welfare and environmental concerns, has evolved into an overwhelming trend. We are also targeting opportunities around agricultural breeding and nursing, designed to increase crop output, as well as flavour and ingredients suppliers with strong development potential.

Covid-19 has amplified many of the themes in our focus areas. In particular, there are two types of assets that are well equipped to foster growth: businesses that are enabling the shift towards a more sustainable world, and tech-enabled companies.

Identifying long-term investment themes in the technology sector is inherently challenging. By definition, technology reinvents the future, and so relying on preconceived frameworks is inhibiting. We therefore ensure that we view the opportunity set from multiple angles. First, we consider which solution category is yielding strong value propositions by driving productivity for end users. We then look at which underlying technologies are at the right stage of the adoption curve, from the user experience to the underlying hardware. Finally, we look at the customer universe and consider which customer sets are at a technology-purchasing inflection point.

By viewing the market through these multiple lenses, we are able to uncover long-term trends that are supported by our digitisation and automation and 'New Living' giga themes, and target technologies which have broad adoption and long-term use cases. This approach has resulted in the identification of several potential investment opportunities, including small and mid-sized business digitisation, outsourcing applications and robotic process automation, which lie at the heart of the digitisation trend. Similarly, we have identified attractive segments that lie at the intersection between the digitisation and automation and New Living themes, including new payments, e-commerce enablement, IoT, digital engineering and digital marketing.

Many transformative trends in the technology and healthcare space continue to be amplified by the pandemic. Valuations tend to be higher in these segments but are justified by strong conviction in the above-average growth outlook.

Elsewhere, we focus on companies that showed resilience during the pandemic and leading companies in fragmented markets are particularly appealing given our strong capabilities in platform expansion strategies. We are selective on growth, where we find many interesting companies but correspondingly high, often difficult to justify, valuations.



"2022 WILL SEE THE DEVELOPMENT OF A MORE BUOYANT BUY-SIDE SECONDARIES MARKET FOR TECHNOLOGY AND HEALTHCARE ASSETS"

JÉRÔME CHEVALIER

FOUNDING PARTNER AND CHAIRMAN, QUADRILLE CAPITAL

Last year proved that a portfolio capable of delivering consistent, cycle-resilient returns requires considered exposure to the technology and healthcare sectors.

Across the year, valuations within these two industries increased markedly and while some investors consider the attractiveness of these spaces to be overplayed, significant tailwinds are set to remain in place in 2022.

The pandemic did accelerate the digitisation of a whole host of industries, however ample room remains for further breakthroughs that can revolutionise how we live, work, and consume. Emerging technologies like artificial intelligence and gene therapy have the clear potential to create value that far exceeds that which stemmed from the advent of the internet. The tech ecosystems in both Europe and China have matured and paired with this, investors' approach to these assets has become more sophisticated – GPs are pivoting away from pursuing disrupters in favour of companies with clear and financed pathways to further growth. That all being said, the context in which technology and healthcare investors operate will continue to grow more complex and we expect some major shifts in this sphere over the next year.

At the end of Q3 2021, 104 buyout funds closed with an aggregated value of EUR88.3 billion, according to Pitchbook, putting 2021 on track to deliver another record-setting year for capital raised. This trend of year-on-year record-breaking in the private markets is set to continue into 2022 and the levels of cash in the market will naturally drive valuation growth.

The extent of this growth is set to be greater than in previous years, with specialist tech funds being raised more frequently and an increasing number of non-traditional operators, such as the hedge funds Tiger and Coatue, entering these spaces, as the cross over funds did before them. The exercise of identifying and securing the right assets will become more competitive, which, in turn, makes the process of de-risking early-stage investments even more complex. In the face of these adverse conditions, investors will seek out the ability to access the best assets through various angles, including via the secondaries market, which we see as an area of substantial growth as early as next year.

Public market volatility, in combination with the need to deploy record levels of capital in increasingly crowded and mainstream private market, is set to focus LP minds on asset liquidity and the exit routes their managers might employ. GPs will need to expand their use of sell-side secondary transactions as a complementary means of realising their investments – this will be especially pronounced among technology and even more healthcare-focused GPs that require to hold and finance their assets over a longer period. Indeed, the agile and systemic use of sell-side secondary transactions will become a more common feature in the market as LP concerns relating to liquidity options and Distribution to Paid-In (DPI) reaches new levels amid a greater level of market risk.

Building on this theme, 2022 will see the development of a more buoyant buy-side secondaries market for technology and healthcare assets. Following a decade-long track record of strength for primary investments, and given the current level of valuations, it appears to be the optimum time for this to occur, as it has in the buyout market.

Looking to the future, it's quite possible that the value of secondaries in tech and healthcare assets will eventually eclipse the value of primary transactions. As secondary transactions are substantially more difficult to source and price than traditional buyouts, investors will progressively seek out specialised and differentiated investment managers knowledgeable of the space.

"NO-ONE KNOWS EXACTLY WHEN A CORRECTION WILL OCCUR, BUT INEVITABLY, IT WILL"



DAVIS NOELL

SENIOR MANAGING DIRECTOR, PROVIDENCE EQUITY PARTNERS

The last few years have brought a flood of capital into private equity, in particular around enterprise software and growth equity technology companies.

As we look forward into 2022, this trend will almost assuredly continue given the massive amounts of capital being deployed to pursue those strategies. The risk here is that anytime there is so much capital chasing the same strategy, eventually the excess return gets priced out of the deals and the overall return profile suffers. No-one knows exactly when a correction will occur, but inevitably, it will, and our goal is to continue to follow a prudent investment strategy that works over the long-term through any market cycle.

We've been sticking to our core sectors of media, communications, education and technology. In order to mitigate some of the risk we see in the market overall today, we're focused on disciplined pacing and diversification of our portfolio. What that means for us is a measured approach to investing, while also looking to generate realisations in our existing assets where possible. Ideally, we seek to invest at a steady pace over a four-to-five-year period. This is a contrast to others we've seen in the market who are investing over half their available capital in the last twelve months alone. At the same time, realisations in our older investments have allowed us to take advantage of the current markets. We have managed our portfolio with a goal of being effectively market neutral, seeking out the best companies and helping them grow.

To build a diversified, robust portfolio, we have tried to balance our investments across our areas of strength. We look to deploy capital across North America and Europe to find attractive investment opportunities at any given time. We also seek diversification across our four sectors. We try to identify the right long-term growth themes and then pick the best management teams and companies that fit those themes. Even though certain parts of the market might be expensive, in our view there are still great companies in which to invest.

Lastly, we try to pursue a variety of companies, so that every investment isn't correlated to the same themes or key factors. We always keep an eye toward solid growth and profitability, and have a portfolio that is composed of investments acquired at a range of EBITDA multiples. Ultimately, our intention is to buy attractive organic growth companies that we can use as M&A platforms and do that at reasonable prices.

Looking into 2022, we see a continuation of a very active deal market, combined with one of the busiest capital raising calendars in history, as more GPs are deploying capital faster and looking to raise ever larger funds. Our focus is to continue to responsibly deploy capital, build a disciplined and diversified portfolio and remain committed to our core sectors of experience.



"SUSTAINABILITY IS GETTING MORE ATTENTION AND WE SEE MORE MANAGERS SPECIALISING IN THIS AREA IN THE YEARS TO COME"

NIELS BARDELMEIJER

PARTNER, STAFFORD CAPITAL PARTNERS

Due to an abundance of relatively cheap capital and a lack of alternatives, the private equity market is becoming increasingly competitive and expensive. As a result, our concerns have been, and will continue to be, related to the ability of managers to source and acquire the right companies at reasonable prices and subsequently be able to realise the potential value.

For these reasons, it has in general become easier for private equity firms to raise new capital. This also holds for emerging managers and is part of the reason why we have seen an increase in the number of emerging managers in past years.

However, there are differences between emerging managers.

For example, for first-time funds it is generally more difficult to raise capital than for a spin-out or a management team with a joint track record. At the same time, emerging managers oftentimes exhibit attractive characteristics such as strong alignment of interest between the team and the investors, leading to outsized return potential. Therefore, emerging managers have always been an important focus area for us to invest in and with.

We have also seen an increase in sector specialisation in the past few years. This trend continued during the pandemic, with an increased focus on the tech and healthcare sectors in particular. In addition, sustainability is getting more attention and we see more managers specialising in this area. We expect this trend to continue in the years to come.

We have always had a strong focus on sector-specialised managers and we will continue to do so going forward. The healthcare and technology sectors are important focus areas for us as they offer attractive characteristics such as high growth, recession resilience and strong historical returns. Playing in the right sectors increases the opportunity for strong returns. However, winning investments exist in every industry. Finding them and creating real value are the key ingredients to success and requires both deep knowledge of sector dynamics and a clear strategy and proper execution by the management team

Due to the persisting disruption, we expect continued interest and competition for deals in these sectors. In our view, deep sub-sector expertise, a strong conviction about the path towards value creation and extensive networks have never been more important.

Although there are many topics that are addressed by LPs during fundraising and deployment, key issues are the alignment of interest between LPs and the GP, and discipline.

On the back of the strong performance of private equity in recent years and a lack of alternatives, there is an abundance of available capital, there is strong tendency to shorten the time between funds and raise bigger funds. This raises concerns related to pricing discipline, potential strategy drift, valuations, and the ability of a manager to generate the same returns as in the past. It is therefore more than ever critical for LPs to remain disciplined when it comes to the selection of funds and challenge the GPs on all of these aspects. Once invested, it is important to stay close to the GPs to ensure they remain disciplined and stick to the strategy in order to be able to generate value and realise strong returns.

Another common question for GPs which will continue into 2022 is related to how they incorporate environmental, social and governance (ESG) considerations in their investment process.

To be more precise, GPs are expected to be a signatory to the UN Principles for Responsible Investment, have an ESG policy in place, monitor and report on the most relevant ESG KPIs for their portfolio companies and assess their contribution to the UN Sustainable Development Goals (SDGs).

Since the EU SFDR regulation came into effect in March 2021, European GPs are also required to provide more detailed sustainability disclosures at the firm level and at the fund level, if their funds promote environmental or social characteristics or have sustainable investments as an objective. In other words, sustainability and ESG integration will remain high on the agenda of LPs and GPs in Europe.

"WE SEE MEANINGFUL OPPORTUNITIES TO DEPLOY CAPITAL IN ASIA-PACIFIC THROUGH THE REGION'S ENERGY TRANSITION AND SHIFT TOWARD RENEWABLE ENERGY"



HAJIR NAGHDY

SENIOR MANAGING DIRECTOR, STONEPEAK

As a global investor in essential infrastructure, Stonepeak takes a thematic approach across target sectors where we believe tailwinds are strongest.

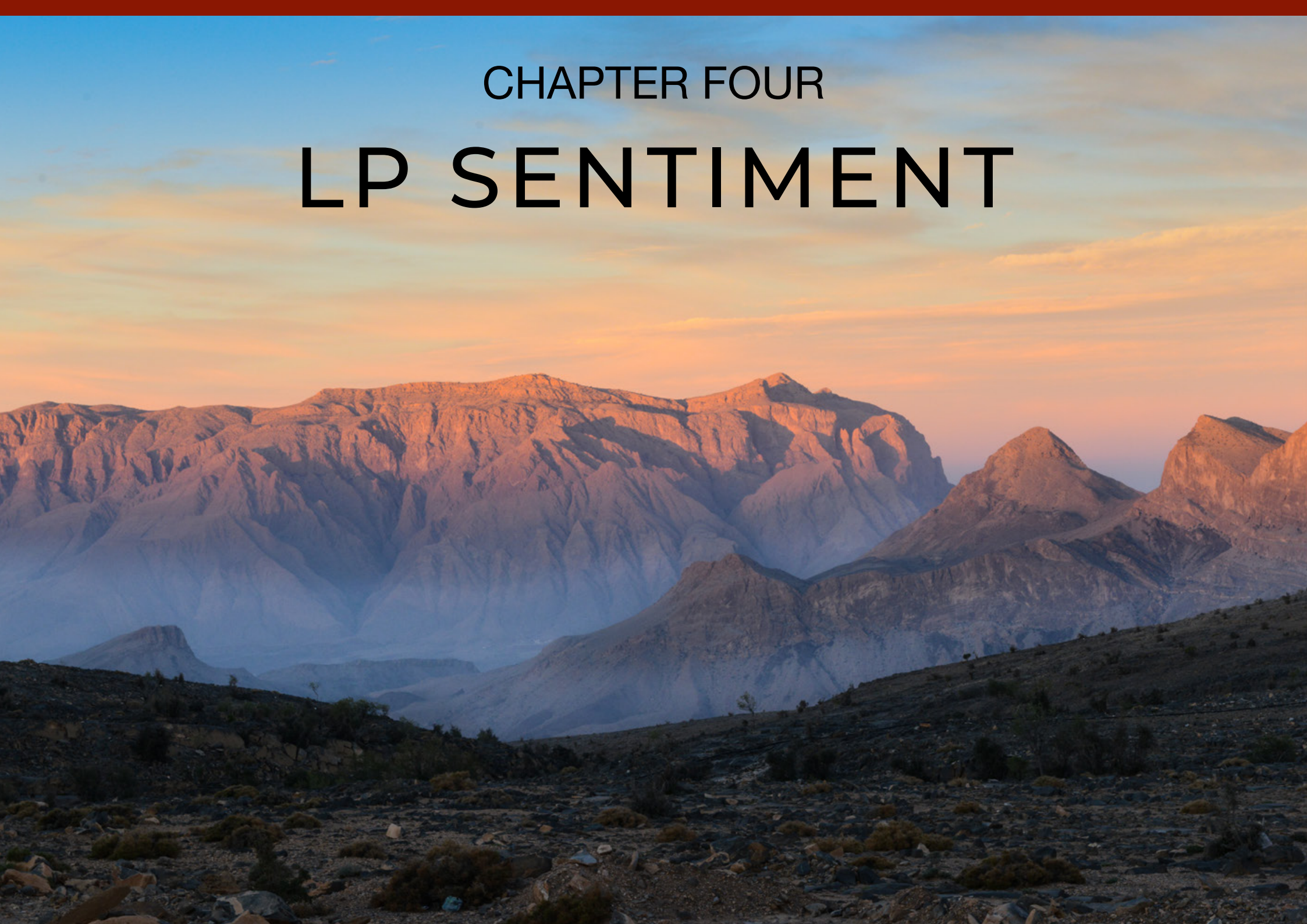
Heading into 2022, we continue to focus on trends impacting three key areas: energy transition and renewables, specialised logistics and digital infrastructure. While the macro trends underpinning these sectors are attractive globally in our view, we see Asia as a particularly compelling region in which to deploy capital and expect interesting opportunities in the year ahead.

We believe that the global energy transition and shift toward renewable energy presents one of the most significant opportunities for private capital investment this century. We are seeing meaningful opportunities in this sector in Asia Pacific, where governments are pushing ambitious energy transition rollouts and placing serious policy focus on new technology. Electric vehicles, hydrogen (with 80 per cent of the APAC economies setting a national hydrogen strategy), offshore wind, and LNG as a key transition fuel displacing coal in the region are trends we are actively following.

Another area of rapid change and opportunity that we are seeing is communications and digital infrastructure. The number of regional internet users, networked devices, and fixed broadband subscribers continues to increase meaningfully year over year, driving significant demand for data centers and mobile infrastructure. APAC is set to continue to outpace North American and European markets in data growth and digital infrastructure demand.

Growing GDP and consumption trends in APAC are also catalysing the continued build-out of the logistics sector in the region with APAC expected to drive 50 per cent of the world's consumption by 2030. E-commerce is playing a major role in the need for more logistics infrastructure: six of the top 10 fastest-growing e-commerce countries are in the APAC region. Modern logistics capacity needs to increase by anywhere from 50 per cent to 10 times in key Asian markets, requiring substantial investment.

Outside of Asia, as we think about other important areas of potential opportunity and challenge for sponsors in the year ahead, we see ESG and addressing pressing issues related to decarbonisation as critical to maintaining license to operate. GPs must have an increasingly sophisticated and fulsome view of the specific ESG challenges across their portfolio and a clear plan to measure and improve the ESG performance of their assets over time in line with net zero ambitions. 2022 will be an important year for sponsors across asset selection and management, measurement, and reporting as many continue to evolve their policies and processes amid increasing pressure from LPs and other stakeholders to demonstrate more meaningful contributions toward global solutions for climate change.



CHAPTER FOUR

LP SENTIMENT



"AS COMPANIES STAY PRIVATE FOR LONGER, INVESTORS MAY SEEK EXPOSURE TO HIGH-GROWTH COMPANIES BEFORE THEY GO PUBLIC THROUGH AN IPO"

MARC SYZ

CO-FOUNDER, SYZ CAPITAL

Financial history will remember 2021 as an extraordinary year for risk assets. Even if less visible than public markets, the year was significant for private equity, in terms of deals closed, valuations paid, and exits, including high-profile technology IPOs.

Moving into 2022, we expect growth to remain healthy, but much of this is already priced in. Asset allocators will need to position themselves intelligently to capture the idiosyncratic returns that private markets can generate and not be misled by an apparent portfolio diversification that often simply doubles down on expensive risk premiums already present in their public portfolios.

Private markets enlarge and enrich our investment universe by offering investors access to attractive assets and companies that are not available in the public domain. They also allow investors to take a longer view, while avoiding the pitfalls of short-term thinking and poor decision-making when faced with market-to-market volatility.

Less efficient private investments can reward diligent investors for thorough analysis and well-executed value creation plans. Finally, they allow investors to participate in success stories before such growth normalises.

Cryptocurrency aside, we expect the Nasdaq to be the clear winner of 2021. As success attracts success, most investors plan to increase their exposure to technology, but also realise that listed tech companies are only the tip of the iceberg.

As companies stay private for longer, investors may seek exposure to high-growth companies before they go public through an IPO. But the more they wait, the more valuation risk increases, especially in today's cash-flooded environment. On the other hand, early-stage investing includes significant business and duration risk, which can only be mitigated through adequate diversification and the availability of follow-on capital.

The right balance is probably somewhere between the two, but access to such opportunities requires specialised skills and networks. Building a private market portfolio to spread risk across vintages takes time and discipline. No crisis or euphoria should side-track investors from achieving their strategic asset allocation goals. However, depending on the macro environment and valuation landscape, allocators may favour some more attractive segments.

When there is ample liquidity and intense competition for deals, we spend time and resources on succession issues in family businesses, or disposing of non-strategic assets. Complexity and small transaction sizes enable us to enter deals at more reasonable valuations, limiting our capital at risk. In the context of market cycles, distressed investing is interesting. Record amounts of money were raised in the darkest days of the lockdown from a wide range of global allocators. Some were disappointed by short-lived opportunities with shallow volumes.

Very few investors had time to accumulate quality assets at low prices before the first vaccines, and subsequent recovery hopes killed the trade. Nor did the anticipated bankruptcy wave materialise either, as moratoriums were imposed in most jurisdictions, preventing companies from filing. As these are lifted, selective opportunities may arise. Despite this, we managed to take advantage of crisis-generated opportunities throughout the year, especially in our litigation funding strategies where we finance an increasing number of insolvency and business continuity claims. We believe this is one of the most compelling ways to benefit from the crisis with no market exposure, and is another good example of diversification.

Meanwhile, we see value in alternative UCITS funds. Their lower expected returns, mainly due to less leverage and concentration than classic hedge funds, are compensated for by better liquidity. This flexibility allows us to be more trading-oriented when managing an alternative UCITS fund portfolio. Finally, we remain convinced of the value of convertible arbitrage and merger arbitrage strategies that can provide diversification, due to their lack of correlation with the wider market.

"INVESTORS MUST APPROACH VENTURE CAPITAL WITH CAUTION, PARTICULARLY THOSE NEW TO THE ASSET CLASS AND LACKING EXISTING RELATIONSHIPS"



ANNA MORRISON

SENIOR DIRECTOR, PRIVATE MARKETS, BFINANCE INTERNATIONAL

Strong secular trends will support growth in impact private equity in 2022 and beyond, with increased accountability at the corporate level for net zero commitments and PRI signatory status, for example, coupled with ongoing and increasing regulatory requirements.

There is more clarity that impact investment is no longer a concessionary asset class, which clears one hurdle. LPs are now moving onto different considerations, such as where impact strategies fit within portfolio construction.

We are also seeing a number of traditional fund-of-funds groups raising funds dedicated to impact investing, alongside a group of specialised providers. This speaks to the growing maturity of this segment.

Among specialist managers, we are increasingly focused on the impact sector as a growing area of interest for clients. The expanding, broad range of investment options and providers position this sector as a sensible addition to a diversified private equity portfolio.

We are also witnessing increased investor appetite for venture capital given the strong performance of this asset class over recent years and particularly during the pandemic. This space must be approached with caution, particularly for those investors who are new to the asset class and lack existing relationships. This area of the market is best addressed initially with the help of specialist fund of fund providers, so we expect to see continued demand in this space.

We also envisage continuing high demand for secondary strategies, both from investors with established private equity programmes and those new to the asset class. Newer entrants to private equity find this space particularly appealing, due to the reduced j-curve, the faster path to a highly diversified portfolio (vintage, geography, strategy) and the earlier distribution profile. The maturity of the secondaries sector has also helped to address some of the traditional pain points felt by LPs in standard fund of fund models.

We've seen a shift in global fund-of-fund allocations, with managers moving away from primaries (although this generally remains the largest overall allocation) and towards larger allocations to co-investment and secondaries. As well as allowing fund-of-funds to provide investors with a more 'secondaries-like' cash flow profile, these give managers more opportunity to gather performance fees, since the market is moving away from charging performance fees on primaries.

Over time, we see knowledge transfer forming an important part of the offering from fund-of-funds, and expect this to continue into 2022. Knowledge transfer capabilities have come a very long way in the past decade, and demand from our clients continues to increase, particularly for first-time investors who wish to build out programmes, and investors seeking to insource management gradually over time.

Many fund-of-fund managers have now acknowledged that knowledge transfer needs to be part of their servicing in order to remain competitive and that this should be highly tailored – even for smaller investors. This can range from tailored education services right through to providing GP introductions and direct access to funds outside of the existing fund of fund relationship.

"WE EXPECT IMPACT PRIVATE EQUITY TO BE OF INTEREST TO DIFFERENT SUB-ASPECTS OF THE CLIENT BASE, INCLUDING ENDOWMENTS AND WEALTH MANAGEMENT"



NICK SAMUELS

HEAD OF MANAGER RESEARCH, REDINGTON

Instead of looking to race onwards like other funds in the sector, we're simply looking to find the best ideas in 2022. We have a 25-person manager research team, which is large by industry standards. We've really invested in our research to make us stand out and we try to hire people from within the industry.

We look for practitioner experience so that the person can bring their industry knowledge while learning about how to conduct manager research. So, when they're talking to a fund manager, they speak and understand their language, as well as the markets themselves, and they understand where fund managers might be looking to pull the wool over your eyes. We employ people who used to be high-yield fund traders, rates traders, and previous chartered surveyors.

In 2021, we saw private equity perform incredibly well, and clients like it; it's often as simple as that. We saw a high interest in private credit specifically, which we expect to continue and grow. It's a big theme across our pension fund clients' portfolios, since this part of our client base isn't necessarily interested in private equity as most schemes have an end point. A private equity investment is something that our clients have previously had, but they're not looking to make any new investments in the near future.

However, private debt is different because the cashflow is ideal for a pension scheme. Within this, we've witnessed increasing interest in opportunistic strategies within our client base. We're continuing to research broader private market strategies as well, since we have different sub-aspects of the client base, including endowments and wealth management. Here we expect impact private equity to be of interest, in particular.

This past year, we've done a lot of work on impact strategies to invest in more sustainable solutions. We focused on renewable infrastructure, private equity and private debt impact. We're also working on natural capital and developing that too.

We assess every manager on how well they integrate ESG into their investment process. We've worked on this for a few years, and we've also been thinking about getting all portfolios aligned to net zero. In April 2021, we made a commitment to align all of our client advice to net zero, and to take our own business to net zero too.

In 2022, we're looking to work with the asset management community to encourage them to align their portfolios to net zero. We're trying to impress upon them that all funds should align to net zero, so our advice is not to launch a brand-new net zero version of your existing fund, given all funds will have to get to net zero. We're asking them to get ahead of that if they're going to continue running our client assets. What that means to us is putting in a constructive plan. Are you going to bring about a 50 per cent carbon reduction by 2030 – if so, how are you going to do this and how are you going to engage with your underlying portfolio companies? The conversation is live and is part of a bigger industry trend.

We think allocations to Chinese equities are very sensible; it's very underrepresented in broad market indices and there's a strong top-down story behind allocating to it, as well as a strong bottom-up alpha story. But, quite rightly, clients have expressed their concerns from an ESG point of view. There have been a number of regulation issues, and a lot of negative press. You rarely make money from investing in things which are comfortable, but we've definitely noticed a push-back from clients on these investments in the past year which indicates a reluctance for these types of investments in 2022.

"LPS SEEKING TO SELL PORTFOLIOS OF FUND INTERESTS WILL USE MORE ALTERNATIVE METHODS FOR LIQUIDITY GENERATION"



COLIN MURFIT

DIRECTOR OF RESEARCH, ALAN BILLER AND ASSOCIATES

In 2021, we primarily focused on North American upper-middle market private equity funds, and we'll continue to do so in 2022. We think this market has the most depth from a GP perspective, and we also think the US middle-market is an attractive place to deploy capital from a risk-adjusted return perspective.

Our client demand for private equity remained relatively consistent across the pandemic and 2021. Target allocations have not increased significantly in recent years and over the same period, we've also seen significant amounts of distributions out of our client private equity portfolios. But it's no secret, private equity GPs these days are returning to market at a brisker pace than the historic norm.

We think we will see ongoing growth in single-asset continuation vehicles in the coming year. In addition, one trend I think we may see more of in the future is greater adoption by LPs seeking to sell portfolios of PE fund interests using alternative methods for liquidity generation, rather than an outright traditional portfolio secondary sale. The most notable of these alternative methods for liquidity generation are structured capital solutions, where an owner of private equity fund interests generates liquidity by financing the portfolio (effectively borrowing and using the portfolio as collateral), rather than outright selling the portfolio in a traditional secondary sale transaction. Currently, Whitehorse Liquidity Partners and 17 Capital are the best-known GPs in this subset of the secondary market, but I anticipate we will likely see greater adoption of this alternative solution to a traditional outright sale by more secondary private equity fund managers in the coming years.

In terms of our due diligence process, we place a very heavy emphasis on evaluating portfolio company-level data for the GPs with whom we partner, and we have a robust proprietary database of portfolio company metrics which we request our managers to update every quarter. This includes key operating performance metrics for each portfolio company in their portfolios. Having access to this data allows our investment team members to readily assess the revenue, EBITDA and leverage profile of each portfolio company held in a GP's portfolio, and how those metrics have evolved over the holding period.

In terms of our approach to investing in the asset class, we don't seek to be tactical and time individual subsectors of the market, instead we focus on picking best-in-class GPs who we feel will perform well in an all-weather environment. LPs can't control the market environment, but they do have control over the quality of the GPs with whom they select to partner. Our programme is primarily focused on established GPs. That said, we are certainly open to meeting with emerging GPs and, under the right circumstances, we would not rule out backing an emerging GP.

In terms of whether to invest with sector specialist GPs or generalist GPs, we tend to be fairly agnostic on this question – however we must ensure we are cognisant that we're not over-exposed to any one given sector in our overall client private equity portfolios. There are arguments in favour of generalist funds, but also in favour of sector specialisation. In reality, most generalist funds tend to focus on three to five sectors. These decisions are best made on a case-by-case basis, and there is no right or wrong answer to the question.

We don't explicitly allocate to ESG-focused private equity funds, however, it's certainly an overlay in our process, and we seek to ensure our GPs – and their underlying portfolio companies – adhere to current best practices and behave as good corporate citizens. Our firm is a signatory to the UN PRI.

"RECENT SIGNS SHOW A BETTER BALANCE OF SUPPLY AND DEMAND ON SECONDARY MARKET PRICING FOR INVESTORS"



TODD SILVERMAN

PRIVATE MARKETS CONSULTANT, MEKETA INVESTMENT GROUP

JOHN HAGGERTY

DIRECTOR OF PRIVATE MARKETS INVESTMENTS, MEKETA INVESTMENT GROUP



As we look ahead to 2022 and despite expected continued uncertainty and inflated asset values, more than anything else we expect to stay the course. We recognise that private equity is a long-term asset class and believe investors are generally best served by maintaining a long-term view, and not trying to time the market. With the growth in fund sizes, accelerated deployment, greater competition, mounting dry powder and high prices, we are doubly focused on risk and ways to mitigate it, via hands-on capabilities, alignment with GPs and pricing discipline.

Investing with top managers remains critical, and many of the traits we seek in those managers have not changed – these include team continuity, strong track records, defensible advantages in the market and a demonstrated ability to add value. Managers themselves must remain nimble and willing to evolve. The successful firms of tomorrow will innovate and find new ways of adding value with specialists in recruiting, capital markets, and other areas.

Though we still see room for generalist strategies, we consider sector expertise as logical and appealing in an increasingly competitive market. This is particularly true in niche, regulated and trend dependent sectors like healthcare, technology and consumer. We remain interested in venture capital strategies, including life sciences, and expect technology to drive investment opportunities and returns, supported by accommodative public markets, and despite lofty valuations.

Of course, we will always need to adapt to new opportunities and challenges. Capital deployment continues at a rapid pace and fundraising cycles are compressed. Previously, GPs typically raised new funds every four or five years, but today they may return to market after two years. As a result, some investors may seek to revisit exposures and focus attention on a select group of core managers.

Additionally, exceptionally strong private equity performance over the past 18 months has many programmes at the top of their desired allocation ranges. We expect this to further the trend towards finding liquidity solutions – either through GP-led fund restructurings, or more targeted use of the secondary market. Until recently, secondary pricing seemed to largely favour sellers over buyers. More recent signs now show a better balance of supply and demand.

Lastly, we see increasing opportunities for LPs who focus on ESG factors in their research and on emerging managers. ESG is no longer a specialised part of the market, but rather it's recognised, at both the investment strategy and firm level, as an avenue through which to create value. Similarly, emerging managers are the future of the industry and very often offer better alignment with LPs with respect to economics and motivation. While the desirable characteristics for successful managers have not changed, the profile and composition of those teams will continue to evolve. As always, relationships and manager selection remain paramount.

Overall, we enter 2022 optimistic for the future, cautious of the challenges ahead, and confident that the long-term view and approach will continue to pay off for investors.

"WE FOCUS ON THE LOWER MIDDLE-MARKET, INVESTING IN SMALLER FUNDS, WHERE THERE ARE FEWER FIRMS COMPETING FOR DEALS AND COMPANIES "



CARLIE EUBANKS

INVESTMENT DIRECTOR, VERGER CAPITAL

TAYLOR JACKSON

INVESTMENT DIRECTOR, VERGER CAPITAL



No one can accurately time the private markets. Our goal is to be consistently invested in top funds over time, across sectors and vintage years, and throughout market cycles. This requires that we develop relationships with top firms early and continually cultivate them to give us access when those firms are back in the market.

Within private equity, we tend to focus on the lower middle-market, investing in smaller funds, typically those sized USD1 billion or below. We believe this area of the market is less efficient, with fewer firms competing for deals and companies that are at the size and stage where managers can truly add value by professionalising and preparing them for the next level, such as acquisition by a larger private equity firm or strategic buyer.

With regards to venture capital, our emphasis is skewed toward early-stage funds that are often led by former founders and operators themselves. We believe these individuals possess the skills to support their start-up companies from an idea, through product development, team building, market identification, and scaling the company to exit.

Valuations are at all-time highs, and the secondary marketplace is no exception. Private equity secondary markets are fully priced, and the spread between venture capital secondaries and private equity secondaries is tightening. We expect to see this continue into 2022, as more investors seek venture capital exposure.

We look for managers who have a unique edge in creating value and who grow their portfolio companies in a consistent and repeatable fashion, regardless of whether the firm is specialised in a specific sector or works more as a generalist.

We have a track record of investing with emerging managers, including many first-time funds, which we expect will continue. We are always eager to identify new talent and opportunities that are differentiated from our existing manager relationships. However, new or emerging managers must compete for allocation with more established firms with longer track records and histories of success. In our review and selection of managers, an emerging manager goes through the same rigorous underwriting process as an established manager.

We start with the view that the consideration of ESG issues in our business and investment decision-making is consistent with our duty as a fiduciary and consistent with what our clients expect of their OCIO. As an OCIO, we allocate capital to external managers. Before hiring a manager, we perform substantial research to determine if the manager has the skill required to provide the desired investment outcome. Environmental, social, and governance (ESG) dynamics can influence the risk and return characteristics of a manager's strategy. Adding an assessment of ESG factors into our manager research process, with a materiality-focused approach, gives us a more thorough understanding of the complex issues and drivers of risks that may impact our managers' portfolios over time. We believe this allows us to make better investment decisions. Because we invest in a manager and not simply in its strategy, our research includes an assessment of a firm's operations and culture. Here, too, environmental, social and governance issues could influence the manager's ability to build and manage a sustainable business, so we consider ESG issues in our operational assessment.

Overall, we are focused on engagement with our managers, which recognises the adverse ESG qualities in a manager's investment strategy or operations and the potential for improvement and growth, and creates plans to work with these managers rather than to not initiate or terminate an existing relationship.

> "OUR FOCUS REMAINS TO IDENTIFY THE GROUPS THAT HAVE A FUNDAMENTAL REASON TO ACQUIRE A COMPANY AND REALLY IMPROVE IT; THEY PLAY AN ACTIVE PART IN THIS AND HAVE OPERATING NETWORKS IN PLACE TO MAKE THE COMPANY GROW. "



CHRIS SHELBY

DIRECTOR, PRIVATE MARKETS, VERUS

We deploy a little over USD2-3 billion per annum across private markets, including private credit, private real assets, real estate, and private equity (which also comprises venture capital and growth capital). Private equity is always topical with our clients, but often for differing reasons.

Leading into the pandemic, interest in private equity was very high because we were seeing expected returns of the traditional markets continuing to decline, and a very low interest rate environment, as well as liquid equity markets which have remained strong over the past decade.

Within buyout and venture capital strategies specifically, we have witnessed a rapid increase in exposure to technology-based companies, given their prevalence across many end markets. In some cases, this has debatably resulted in an overweight to technology. We are aware of this exposure and in many cases are seeking to find opportunities that may be less correlated to the valuation factors of technology companies. Our focus remains to identify the groups that have a fundamental reason to acquire a company and really improve it; they play an active part in this and have operating networks in place to make the company grow.

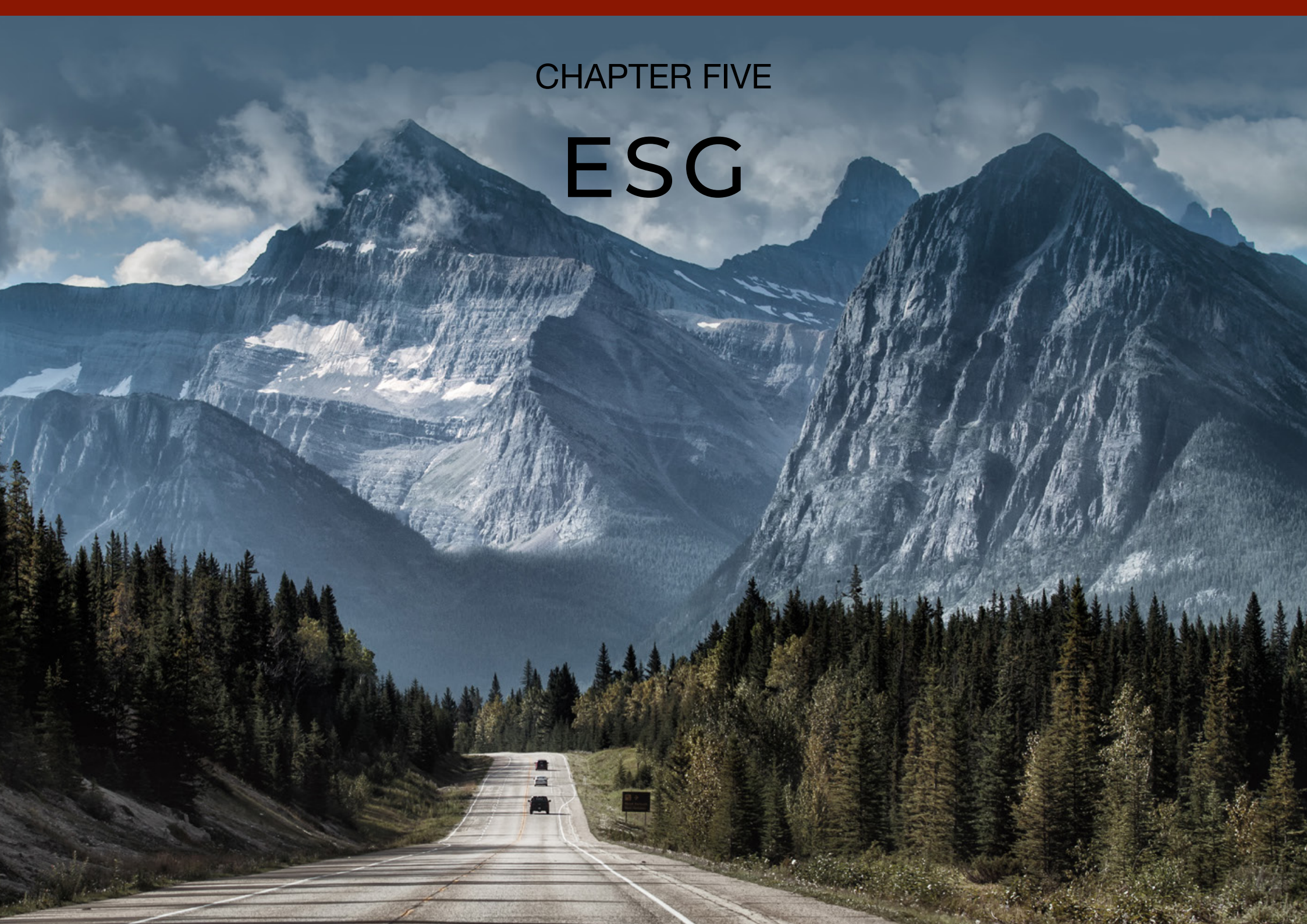
Private credit is an area where we've seen a tremendous amount of interest, in part because of the lower interest rate environment and tight spreads offered in the traditional fixed income markets. Portfolios that entered the space as a yield enhancement to traditional fixed income are looking to broaden their exposure to a diversified mix of strategies. These may include more opportunities strategies, as well as those that may offer an element of diversification from a collateral perspective. As many clients have grown to include distressed debt strategies within a private credit portfolio, we've found that this space may experience headwinds due to the tremendous amount of additional capital that has been allocated to the space in recent years, combined with the somewhat benign market conditions. Opportunities remain in strategies seeking to provide transitional or situational capital to companies that may be suffering from an idiosyncratic event.

Private credit portfolios are also considering more niche and possible credit-like strategies including royalty-based strategies, litigation finance strategies, portfolio finance, and various other real asset lending strategies. These typically have very different return and risk profiles from traditional corporate-focused strategies but may offer an enhanced level of diversification at the portfolio level.

With regards to ESG, these standards are incredibly important to Verus and to our clients. We integrate an ESG evaluation into the initial screening of private markets firms, followed by a thorough review in further diligence. However, we're aware that you must be wary with ESG, because many will approach the topic and claim to adhere to the principles, but ultimately their portfolios may not back this up. Additionally, sound adherence to ESG standards does not necessarily result in the achievement of excess returns, therefore the diligence process must balance the ESG review with other investment criteria.

CHAPTER FIVE

ESG



"GPS WITHOUT ANY INTERNAL ESG EXPERTISE WILL BECOME EVER MORE RARE IN 2022"



COLIN ETNIRE

HEAD OF ESG, BC PARTNERS

Climate change is rightly the most important theme for investors, both because it's a fundamental existential issue, and one where investors' ability to understand and integrate it into decision-making is rapidly maturing. Over the past year, most of our portfolio companies now calculate their own greenhouse gas (GHG) footprints, and we will continuously work toward improving our data quality and completeness after signing onto the Portfolio Carbon Accounting Financials framework. If a company is not taking at least initial steps towards reducing their footprint in 2022, it will rapidly be left behind.

In 2022, we expect a continuation of what we've seen in 2021: GPs without any internal ESG expertise will become ever more rare; large GPs will grow their teams to something more capable of managing their portfolios; and more ESG issues will be taken seriously by other functional areas, such as compliance. It will become more institutionalised, and less peripheral. Five years ago, ESG was put in the same bucket (in compensation, in organisation chart, and in the minds of leadership) as marketing. Now, it's an essential operational function.

In terms of funds, we believe that the traditional structure will persist, with ESG-linked financing or explicit impact mandates proving to be more of a fad than a long-term revolution. We've always said "good ESG is just good investing," and we expect that to lead to a convergence with traditional investing as the logical endpoint.

Luckily, we have had almost no historical exposure to fossil fuels, which is the sector where an ESG-driven transition is most obvious. However, there are certain carbon-intense sectors, such as cement production and some areas of agriculture, that are not directly linked to fossil fuels. As more businesses conduct GHG footprints, investors will become more aware of other high-risk sectors, which will then be pushed toward transitional paths of their own.

Over the five years I've been in private equity, there has been a notable change in the level of sophistication in the questions LPs ask regarding ESG. It's no longer just policies, it's no longer just personnel. Where it gets harder is when LPs push questions through to outcomes and performance. To some extent, that's centering on quantitative elements such as KPIs, although that can't measure everything. The most sophisticated questions we get are when LPs stress-test our ESG approach via specific portfolio companies, since that approach reveals which GPs merely have nice policies or case study highlights, and which GPs really have a strong ESG baseline across the board. I believe that's an area that BC Partners compares favourably to its peers.

Through 2022 and beyond, a regional split in ESG regulation is certainly developing. The EU is trending towards specific mandated reporting and classification, while the US, via SEC enforcement, is focused more on holding firms accountable for whatever promises they themselves make. Canada and the UK are both considering their own regimes.

To me, this represents an adolescent stage of ESG development: welcome, but not without awkward transitions. Ideally, in the long run the regulatory frameworks will take a back seat to sophisticated LPs deeply understanding their ESG preferences and making allocation decisions based on it. That will lead to a more competitive ESG world than we have today, but that's a necessary development if we ever want ESG to deliver on its promises of solving global challenges.

"THERE IS A REAL PROBLEM WITH ESG DATA – WE DON'T HAVE CONSISTENCY AND WE DON'T HAVE AUDITABILITY OF WHAT IS REPORTED"



TED HOLMES

FOUNDER, BLUE OCEAN INVESTMENT PARTNERS

ESG is a core part of understanding our risks on a long-term basis, but there is a real problem with the data.

On a global level, we don't have consistency and we don't have auditability of what is reported, so the data is very sketchy on an underlying basis. On top of that, a lot of people are using scorecards and I have some fundamental issues using scorecards: the main one being that a critical issue for one company (that would from our standpoint make them un-investable) might get lost on a scorecard.

It comes down to the consistency and comparability of data and how it gets integrated into a scorecard and reported out.

You can have the same company and look at six different scorecard providers and get some very different answers. So a lot of this is still in the early stages. We need to look at the data going into these systems and the scorecards that come out. I think it's important to investigate the individual companies and the individual issues and identify what are the critical long-term risk factors. The scorecards can miss that, so there is a real issue there.

It comes downs to the ESG team looking at the data and the scorecard and saying, "Oh you bought this thing that was a D-" and the portfolio team and the analysts saying, "Yes, but this is a really good return profile, so we are going to buy it anyway", and so you get this disconnect. A firm can claim to do certain things, but if you look at the underlying data some are still holding things that look like the benchmark for lots of dirty companies.

I would also say, if you're a large firm it's easy to have the resources to report if you're Article 8 or Article 9 [on the EU's SFDR]. If you're a small firm, even though you are clearly Article 9, you are saying you are Article 6 because you just can't afford to do all the reporting that's required. So there is this interesting dichotomy in the market between the larger and smaller firms.

From the underlying data point of view, one of the most interesting things to come out of COP26 was IFRS announcing the international sustainability standards board. We're aware of what they have done on the accounting side, so if they can do the same on the sustainability side with some base case numbers, that will really help.

"SUSTAINABLE INVESTING AND THE FOCUS ON ESG IMPACTS NEED TO BE SEEN AS THE NORM ACROSS THE PRIVATE EQUITY INDUSTRY"



AVENT BEZUIDENHOUDT

HEAD OF INVESTMENT, EARTH CAPITAL

Over the past two years there has been significant focus on integrating ESG guidelines into responsible investment processes. This focus was intensified by virtue of COP26 – especially in relation to the financial markets and the promises made by investors to deliver net zero in line with publicly made commitments and time horizons.

The delivery of these necessary but challenging targets can be significantly advanced by the private equity sector, where investors have greater influence over the strategic decisions made by portfolio companies than they would in the public markets. Therefore, we expect that 2022 will see ESG considerations becoming central to investment decision-making and will drive private equity processes.

We believe that LPs' focus will be on ensuring that their money is being utilised effectively to deliver their net zero ambitions, while maintaining strong financial returns and making a meaningful impact. This will require the private equity industry to be truly transparent with its achievements, and work towards a model framework for providing the appropriate measurement data so that investors can understand how their funds are being deployed to improve businesses and make industries more sustainable, as well as allowing for real performance comparisons between fund managers.

As the devastating effects of climate change continue to be felt around the world, we will be looking to the innovators to find novel solutions to address these issues, and to the finance sector to provide the necessary resources to ensure these businesses are funded and can grow sustainably. The emergence of climate tech businesses must be encouraged, with more investors focusing on these critical solutions.

The ongoing outbreak of Covid-19 has shown how our reliance on "business as usual" has faltered, with increased concerns for food, water and energy security, and the effects on our society and environment becoming significant considerations for future asset allocation. The emergence of the Omicron variant in late 2021 has further shown that the pandemic is far from over. Despite the ongoing rollouts of the vaccination programmes around the world, Covid-19 disruptions and lockdowns are likely to continue throughout 2022, making business planning difficult and delaying decision-making. It will be vital for companies to be well-financed to weather the storms, and for them to be sufficiently nimble to react quickly to changes as they happen. Strong management teams have always been a key factor for investors, but now this will be more important than ever.

Sustainable investing and the focus on ESG impacts need to be seen as the norm across the private equity industry, with a focus from investors on delivering a just transition as we drive towards net zero. The current debates around reporting, transparency and delivering a market standard must also continue if we are to achieve real change. This will take commitment and co-operation from all stakeholders but, if successful, will ensure that funds continue to flow into impactful opportunities and that the private equity sector drives the right decisions.

"COMPANIES WHO COME UP WITH SUSTAINABILITY CLAIMS BUT HAVE NOTHING TO BACK THEM UP ARE AT RISK"



VIVEK BAPAT

SENIOR EXECUTIVE, SAP

Sustainability trend lines across 99 per cent of every industry are upward for C-Suite sentiment for sustainability, meaning that it's an important factor to most industries, from media and entertainment to biotech and life sciences.

The real challenge of the moment is going beyond aspirations related to sustainability, which might be three, five, 10, or even 30 years away, and moving towards the activation of sustainability across core business activity.

The focus of business leaders should now be to ensure that there is no "authenticity gap" between aspiration and activation, and that companies don't communicate something without a clear, well thought-out operational plan. From a brand perspective, companies who come up with these claims but have nothing to back them up are at risk in terms of their authenticity and purpose-washing, exposing themselves to substantial erosions of brand equity.

One of SAP's recent studies, of more than 3,000 companies globally, showed that, in the context of financial reporting and thinking of sustainability as a material aspect of a company's profit, only 17 per cent strongly believed that the impact of sustainability was immediately financially relevant to their business performance. This group, which we called the 'Nows', were quick in enacting sustainability-led operational transformation as a clearly designated business priority across their core business. However, 22 per cent felt that sustainability was imminent and relevant but wanted to take a 'wait and watch' approach. A further 61 per cent wanted to see how this affected other companies first before enacting anything themselves.

In the 17 per cent group, we found that sustainability has been driven from the top down – from the C-Suite or, in many instances, as a board mandate. This was a counter-intuitive finding, as most of the external coverage of sustainability issues is related to employee and consumer activism. Clearly in many firms, we believe that the C-Suite is in a leadership position to drive sustainability transformation in a big way – just like with digital transformation in the past.

We also identified the operational challenges of driving sustainability.

Seventy-nine per cent of companies surveyed were dissatisfied with the quality and access to the right financial and non-financial data required to drive sustainability transformation. This means that the scope of data is at the heart of the sustainability movement in terms of trying to solve this issue.

But this isn't the only problem; another issue is driving sustainability at scale. Companies want to drive sustainability at scale by embedding these data insights and driving them into their core business processes, whether it's procurement, supply chain, finance, or recruitment. The common understanding is that sustainability can't be a side-car project, it must be brought into the core of the business for progress to be made at the relevant scale and speed. One third of companies in our survey did not know how to integrate sustainability into their core business strategy, systems, or processes.

We also found that the higher the level of digital maturity, the better a company's ESG performance has been and will continue to be. The opportunity for companies to move and accelerate into sustainability transformation at scale readily exists for those already invested in digital transformation technologies.

"INSTITUTIONS WILL TAILOR THEIR PORTFOLIOS TO ALIGN WITH THEIR MISSIONS AND VALUES, WHICH IS MORE DIFFICULT IN PUBLIC MARKETS"



CHRIS MATTEINI

HEAD OF INVESTMENT RESEARCH, SUSTAINABILITY AND EQUITY-ORIENTATED ASSETS, TIFF INVESTMENT MANAGEMENT

TIFF has incorporated ESG analysis into all its investment decisions since 2017. Since then, we have seen a meaningful uptick in client requests for access to ESG-like strategies. In response, TIFF formally launched its dedicated sustainable investment strategies in 2020. These strategies employ a combination of sustainable investments strategies, including ESG integration, corporate engagement, exclusionary screens, and investment in sustainability themes, such as energy transition, resource efficiency, healthcare and water.

Endowment and foundation clients often ask about sustainability. During our analysis on the mandatory global carbon markets, we reviewed many carbon-reducing technologies and are now in the process of researching energy transition managers. We have European managers and a Taiwanese market-neutral manager who have already formally incorporated ESG into their investment process.

We expect continued growth in ESG product demand and development. While divestment and ESG risk assessment will continue to be widely used strategies, we expect a continued shift toward thematic and impact investments: investing in businesses helping to solve environmental and social ills. We expect climate change and racial equity to continue to be key areas of focus. Engaging with corporates on ESG issues to drive change will also be a key strategy.

Individuals and institutions will tailor their portfolios to align with their missions and values. This is more difficult in public markets, though there are plenty of interesting opportunities to invest sustainably. In private markets, investors can target very specific themes and geographies.

Continued consolidation in ESG reporting frameworks is a positive step. If we are to improve ESG data collection and reporting, we need universally agreed-upon frameworks. The creation of ISSB (the International Sustainability Standards Board) is a great development for this to happen.

"DIVERSITY OF THOUGHT LEADS TO IMPROVED INVESTMENT OUTCOMES OVER THE LONG-RUN"



TARA CLEAVER

INVESTMENT DIRECTOR, CREWCIAL PARTNERS

At Crewcial Partners, our diversity and ESG work has been a priority for several years, and diversity and ESG continue to be important objectives for the firm. We believe that having differentiated perspectives and investing responsibly can have a positive impact on organisations, society and investment returns.

Our diversity and ESG framework is deeply embedded into our firm's culture and research process. We consider diversity and ESG factors in parallel when we evaluate a manager, based on qualitative and quantitative metrics. We also have a member of our investment team who is dedicated to sourcing diverse managers, and another member of our investment team who leads our ESG efforts.

We define 'diverse' as managers that are over 50 per cent owned by women and/or ethnically diverse individuals. We pay attention to the diversity of the talent on an investment team, but the majority ownership is an important measurable characteristic. Approximately 90 per cent of our clients have at least one allocation to a diverse manager, and over 10 per cent of our advised assets are invested with diverse managers.

We have built a robust pipeline of diverse managers over the years and quantify our efforts to ensure that we are continuing to make progress. Diverse manager meetings represent approximately 25 per cent of all manager meetings at Crewcial – that is compared to approximately 1 per cent capital in the industry that is managed by diverse individuals. So, while we may be happy about the progress we have made in this area, there remains a significant amount of work to do. Crewcial believes that diversity of thought leads to improved investment outcomes over the long-run, and that has certainly been the case in our experience. Our outreach efforts have been successful in that we have been able to source talented diverse managers, and the benefits have materialised in our clients' returns.

Crewcial advises endowment and foundations, so ESG has always been important to our clients and, over time, we have seen ESG become increasingly meaningful to them. There is a myriad of sustainable investing approaches that have emerged, as capital owners and allocators discover ways to increase returns and target sustainable investing outcomes. The three primary sustainable investment approaches include ESG, SRI and impact, all of which enhance traditional investment analysis to identify potential risks and opportunities.

ESG (Environmental, Social, Governance) incorporates environmental, social, and governance factors into the investment process, SRI (Socially Responsible Investing) applies positive or negative value/impact screens to determine investment priorities, and impact funds aim to deliver specific and measurable impact goals alongside of their financial return targets. Some clients take this to the next level by including SRI, ESG, and/or impact goals in their investment policy statement. When clients generate superior investment returns while making a positive social or environmental impact, it's a win-win.

PRIVATE EQUITY WIRE