OVERCAST WITH SOME BRIGHT SPELLS

June 2024

Overview

If investors were expecting the private equity market to jump back into action in 2024, they will have been disappointed. After a subdued 2023, overall private equity investment and exit activity in the first quarter of 2024 continued to be challenged. However, there were bright areas in some segments of the market.

For example, in contrast to other regions, Europe showed strong positive growth in activity vs. the same quarter a year ago. Driven by the continued lull in exit activity, the secondaries market recorded its second-best ever year in terms of investment volume. Meanwhile, average EBITDA purchase price multiples are close to five-year lows, likely being pushed down by lower usage of expensive debt. For private equity investors, these are signs to remain optimistic.

Paul Newsome

Head of Investment Solutions, Private Equity

Key Points

1. Activity remained stable in the mid-market but fell sharply at the larger end
2. The secondaries market shows remarkable resilience in the face of an overall difficult private equity market
3. Balancing GP-led deals, single LP-stakes and direct secondaries has the potential to achieve the best outcomes for investors

Mid-market underpins activity

The global aggregate value of private equity deals closed during Q1 2024 was a paltry USD 86bn, 43% down on the same quarter last year[1]. This was driven by particularly weak activity in North America (-49%) and APAC (-72%), while Europe (+106%) rebounded in style, albeit off a very low Q1 2023.

However, while dollars deployed were significantly down, the number of private equity deals closed during Q1 2024 was only 9% down. This suggests that activity remained stable in the mid-market but fell sharply at the larger end of the market. Indeed, the average deal size recorded in Q1 2024 was USD 269m, 40% down on a year ago and the lowest in any quarter for eight years.

This magnified slowdown in activity at the large end of the market can be explained by interest rates remaining at a high level. After over 10 years of hovering around 6%, average LBO loan yields increased to almost 11% in the US in 2023, making buyout deals more expensive to finance[2]. Hitherto, large and mega cap private equity managers have relied on a high proportion of debt in their deals to achieve targeted returns. Thus, with debt much more expensive, they instead require purchase price multiples to fall significantly to maintain similar returns. However, this leads to a stalemate since sellers are preferring to wait than accept lower prices.

Since up to half of exit activity is driven by private equity managers buying from other managers, it is not surprising that exits were also down during this quarter. The global aggregate value of exits was USD 64bn, a decrease of 26%

[1] Preqin, April 2024

[2] Bain Global Private Equity Report 2024

Read more of our latest investment thinking online: www.unigestion.com/insights on the same quarter last year[3]. This decline was driven by North America (-41%), while Europe (+22%) and APAC (+31%) were both positive.

In Q1 2024, in contrast to the market, we have continued to see strong exit activity. In February 2024, we announced the biggest exit so far from our 2016 Direct program. We agreed to sell Atria, a tech enabled wealth management platform for independent broker dealers, to LPL Financial Holdings, a Nasdaq listed national independent broker dealer. This has been a market consolidation play, where the company has made eight significant acquisitions in a highly fragmented market. Since our investment in 2018, the company has grown its revenues from USD 140m to almost USD 900m. The exit, expected to close in Q3 2024, will lead to over USD 80m of distributions back to our investors, and a TVPI of up to 4.6x (3.8x net to investors).

Meanwhile, also in February, we agreed to sell two German companies, Academia and Certania, from our 2020 vintage direct program. Academia is a group of specialist medical laboratories focusing on pathology, human genetics and hematology. Certania is focused on testing, inspection and certification for the food and sustainability industries. We were the initial day one investors in these companies alongside Greenpeak Partners, a German buy and build specialist. Both companies will be exited via a continuation fund, managed by Greenpeak. For Academia, this will lead to a gross TVPI of up to 2.7x (2.3x net to investors) or more, depending on an upside sharing mechanism. For Certania, we will receive proceeds of 2.7x gross (2.3x net) and, since Unigestion will retain a 10% shareholding, the TVPI will be over 4.8x gross (4.0x net to investors).

Finally, we had a very good early exit from our 2021 vintage emerging manager fund of funds program. In February, Spirii, a Nordic provider of end-to-end software e-mobility charging solutions primarily to B2B customers (e.g. charge point operators, car park operators, etc.) to Edenred, a French listed payment service provider. Spirii is a co-investment we made alongside Nordic Alpha Partners less than 18 months ago. Unigestion participated in two successive funding rounds in October 2022 and October 2023 to help the company fund its transition from a turnkey e-mobility solution provider into a leading Platform-as-a-Service tech company. This transaction will return a gross TVPI of 2.5x gross TVPI (2.5x net to investors).

Returns remain positive

Despite feeble activity in the private equity market in recent quarters, average buyout returns have remained positive. In 2023, investors saw average buyout returns of 7.9% for the full year. This ranged from 5.4% for large buyout returns to 12.7% for mid-market buyout returns.

Meanwhile, investors in the public markets have been treated to much stronger returns. In 2023, the MSCI World was up 24%. However, any private equity investor will tell you that one does not invest in private equity for short term returns. Since 2007, annualised buyout returns have been 11.6% vs. 7.1% for the MSCI World, a premium of 450 bps.

It gets even better in the mid-market: since 2007, annualised mid-market buyout returns have been 13.1% - a premium of 600 bps over the MSCI World.

We also continue to see positive performance across our funds, driven by strong revenue and EBITDA growth within the portfolios. For example, in our latest Directs strategy, the portfolio companies have (on average) grown revenues by 27% in the last 12 months, while EBITDA margins grew from 24.6% to 24.9%.

In our Climate Impact Strategy, which we began investing in 2022, one of the standout investments is Carbonfree. This company has developed a technology to capture CO_2 emissions from a variety of hard-to-abate industry processes and convert the

[3] Preqin, April 2024

captured CO_2 into carbon free chemicals such as precipitated calcium carbonate (PCC). PCC is a high-value add product used in the manufacturing of paper, plastics, ceramics, rubber, paints & coatings, pharma and food/nutraceuticals. As such, the company recorded USD 15m of EBITDA in 2023. In Q1 2024, the company won a contract with U.S. Steel to build a second carbon capture installation. Once completed, this will lead to the doubling of the company's EBITDA.

Secondaries on the march

Overall, the secondaries market grew marginally in 2023 (USD 109bn) vs 2022 (USD 102bn)[4]. This made it the second largest annual volume on record, but still some 13% below 2021 (USD 126bn). However, when we dip below the surface, the underlying trends gives us a feel for the market drivers - and a view on the continued outlook for 2024.

Secondaries market volume is trending at an all-time high.
After a slow start to the year, secondaries transaction volume picked up in H2 2023 recording a 57% increase over H1 2023[5]. In fact, H2 2023 volumes imply an annual run rate of USD 134bn, which is above the annual record set in 2021.

Secondaries dry powder remains steady.
In the last three years, dry powder for secondaries deals has oscillated between USD 225bn and USD 250bn, which is close to 2x secondaries investment volume[6]. This compares favourably to other parts of the private equity market (e.g. the same ratio is about 3x for buyouts). Given the continued glut in exit activity, the supply of secondaries deals is bound to remain healthy, suggesting that the market is currently in a healthy equilibrium.

LP-stake pricing was up, GP-led pricing was down.
The average pricing of a buyout fund was 91% of NAV, up from 87% in 2022 (but still below the recent peak of 97% in 2021)[7]. However, the indications are that pricing was lower for GP-led deals in 2023, with 32% of deals reported to be at 10% discount or lower, vs. 20% in 2022[8].

GP-led deals have steadied at around 45%-50% of overall volume.
After growing quickly from 2015 to 2020 from almost zero to 50% of all secondaries, the proportion of GP-led deals seems to have found its equilibrium at around 45%-50% during the last three years[9].

Multi-asset continuation vehicles (CVs) grew the most.
Multi-asset CVs accounted for 38% of all GP-led deals in 2021, up from 31% in 2021[10]. Meanwhile, single asset CVs reduced from 52% in 2021 to 39% in 2023. This is likely driven by certain secondary investors shifting to more diversified portfolios in order to limit single asset concentration risk.

More investors are shifting to the mid-market. Approximately 89% of single asset CVs was focused on deals of less than USD 1bn in 2023[11]. Furthermore, only 33% of mid-market managers surveyed have completed a GP-led transaction, compared to 67% of large cap managers. This suggests that there is more white space in the mid-market.

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[4] Lazard
[5] Lazard
[6] Greenhill
[7] Greenhill
[8] Campbell Lutyens
[9] Lazard
[10] Lazard
[11] William Blair

In single asset CVs, resilient sectors are overrepresented. For example, healthcare is the largest sector amongst single asset deals, representing around 25% of all deals[12]. Interestingly, across all buyout deals in 2023, only 10% were in the healthcare sector.

Taken together, the secondaries market shows remarkable resilience in the face of an overall difficult private equity market. We believe that it represents an excellent time to apply our secondaries fusion strategy – a deliberate balance between GP-led deals, single LP-stakes and direct secondaries - in order to achieve the best outcomes for our investors.

In this environment, more than ever, it is important to build a portfolio of high-quality underlying companies which can deliver the desired cash flow pattern. In our case, we aim to deliver a DPI of 1x to our investors after five years. We also aim to deliver continuous strong and predictable distributions through to the end of each program's life.

Why don't we seek higher diversification and maybe bigger discounts by doing large multi-line LP-stake portfolios? Firstly, in order to achieve 1.8x+ on such deals, it is necessary to use leverage and/or heavy deferral mechanisms. Since leverage needs to be paid back first, distributions would then be delayed, Secondly, large portfolios lead to unwanted "by-catch" – low quality portfolio companies which are tough to exit, further delaying distributions, as well as bringing negative surprises at the end of the program life.

Our fusion strategy is designed to deliver predictable cash flows to our investors by specifically focusing on: (1) no leverage and limited recycling, (2) single line LP-stakes in funds well known to us, (3) short hold GP-led deals, (4) active portfolio management, and (5) direct secondaries to reduce the TER.:

This has led to us delivering consistent, top quartile returns to our investors over the last five secondaries vintages.

Unigestion Private Equity Activity

Here are the highlights of some of the investments that we completed in Q1:

ATRIA Wealth Solutions

In February, Unigestion, together with Lee Equity Partners, signed definitive agreement for the sale of Atria Wealth Solutions, a wealth management solutions holding company, to LPL Financial LL. Atria Wealth Solutions, headquartered in New York, supports approximately 2,400 advisors and 150 banks and credit unions, managing approximately USD 100bn of brokerage and advisory assets. Established in 2017, Atria operates a network of broker-dealer subsidiaries focused on supporting independent financial advisers and institutions nationwide. The transaction is expected to close in Q4 and will result in a TVPI of around 4.4x (3.8x net to investors). Distributions to our 2015 direct program are expected to amount to some USD 86m in total.

Zvoove Spirit

Also in February, Unigestion invested in a multi-asset continuation vehicle managed by German B2B-Software specialist fund manager LEA Partners. The continuation vehicle consists of Zvoove, the European leader of end-to-end ERP and recruiting software solutions for temporary staffing agencies, as well as OneQrew, the market leader in ERP-software for craftsmen in the DACH region. Both players are headquartered in Germany. Zvoove and OneQrew operate a very sticky business model, deeply embedded in their customer's ecosystem through ERP-software solutions which generate mostly recurring revenues. The companies are well-positioned market leaders with an opportunity to consolidate their respective growing, fragmented and specialised B2B software sub-sectors.
In the same month, Unigestion - together with Nordic Alpha

[12] Lazard

Partners - signed the exit of Spirii, a provider of end-to-end software e-mobility charging solutions. These are sold primarily to B2B customers, typically charge point operators, real estate and property owners. Unigestion invested in Spirii less than 10 months ago, helping the company fund its transition from a turnkey e-mobility solution provider into a leading Platform-as-a-Service tech company. Through proprietary technology and a strong partner network, Spririi covers the whole EV charging value chain by offering a cutting-edge EV charging management platform and an intuitive end-use charging and roaming app.

Also in February, Unigestion signed the exit of two of our Greenpeak platforms in Germany - Academia and Certania. Under the ownership of Greenpeak, the two companies have developed into leading diagnostics platforms for specialty laboratories and testing, inspection and certification (TIC) services in Germany. Academia is a leading diagnostics platform with a focus on pathology, human genetics, haemostaseology and prenatal diagnostics in Germany. Certania is a leading provider of TIC services with a focus on addressing global health and sustainability challenges. Academia and Certania have increased their combined EBITDA under Greenpeak's ownership to almost EUR 70m and completed over 30 acquisitions in total. The exits will result in a TVPI of 2.7x (2.3x net to investors) and IRR of 224% for Academia and a TVPI of 2.7x (2.3x net to investors) and IRR of 147% for Certania.

In March, Unigestion invested in US-headquartered PCS Retirement alongside Lee Equity Partners. PCS Retirement, founded in 2001, is an independent retirement plan recordkeeper specialising in serving small to medium-sized business (SMB) retirement plans. The company manages essential aspects of retirement plans, such as tracking plan participants, contributions, distributions, and investment elections. PCS distinguishes itself through a financial adviser-led approach, allowing advisers to customise retirement plans for their employer clients. PCS is headquartered in the Mid-Atlantic region and offers a wide range of retirement plans, including 401(k) and 403(b). It is expected that PCS will have an appealing chance for consolidation in a fragmented market at favourable entry prices, and have the ability to realise synergies.

Unigestion closed a direct secondary investment in Visma during March, alongside Hg Capital. Visma, headquartered in Oslo, is the leading provider of mission-critical software to SMBs and the public sector in Northern Europe (Nordics & Benelux), covering accounting, resource planning, payroll and transaction processing. Visma serves more than 1.6m clients with SaaS solutions. The business offers payroll, book keeping, tax and regulatory compliance software modules to its customers on a subscription basis. These products are used daily, are critical to operations and, importantly, are highly regarded by their customers. The business model's resilience is evidenced by consistent annual organic growth through the GFC and Covid crisis. The company is the Nordic market leader in the growing SMB segment with further penetration potential.

Also in March, Unigestion committed to Iron Path I. Iron Path focuses exclusively on investment opportunities within specialty industrials and healthcare, sectors in which the team has deep expertise, capabilities, relationships, and insights. Iron Path's investment and operating experience within these focus areas uniquely positions the firm to pursue sector-intersecting investments along the value chain from molecule to patient. The fund has already made four platform investments.

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