Diversifikation zählt.

Herzlich willkommen zum BAI-Webinar

„Auswirkungen der Corona-Krise auf die Assetklasse Private Equity“

Einführung: Annette Olschinka-Rettig, Geschäftsführerin, BAI e.V.

Referent: Dr. Nils Rode, Chief Investment Officer, Schroder Adveq

Montag, 30. März 2020

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Weitere Webinare in dieser Reihe:

Auswirkungen der Corona-Krise auf die Assetklasse…..

Hedgefonds (3.4.20)

Private Debt

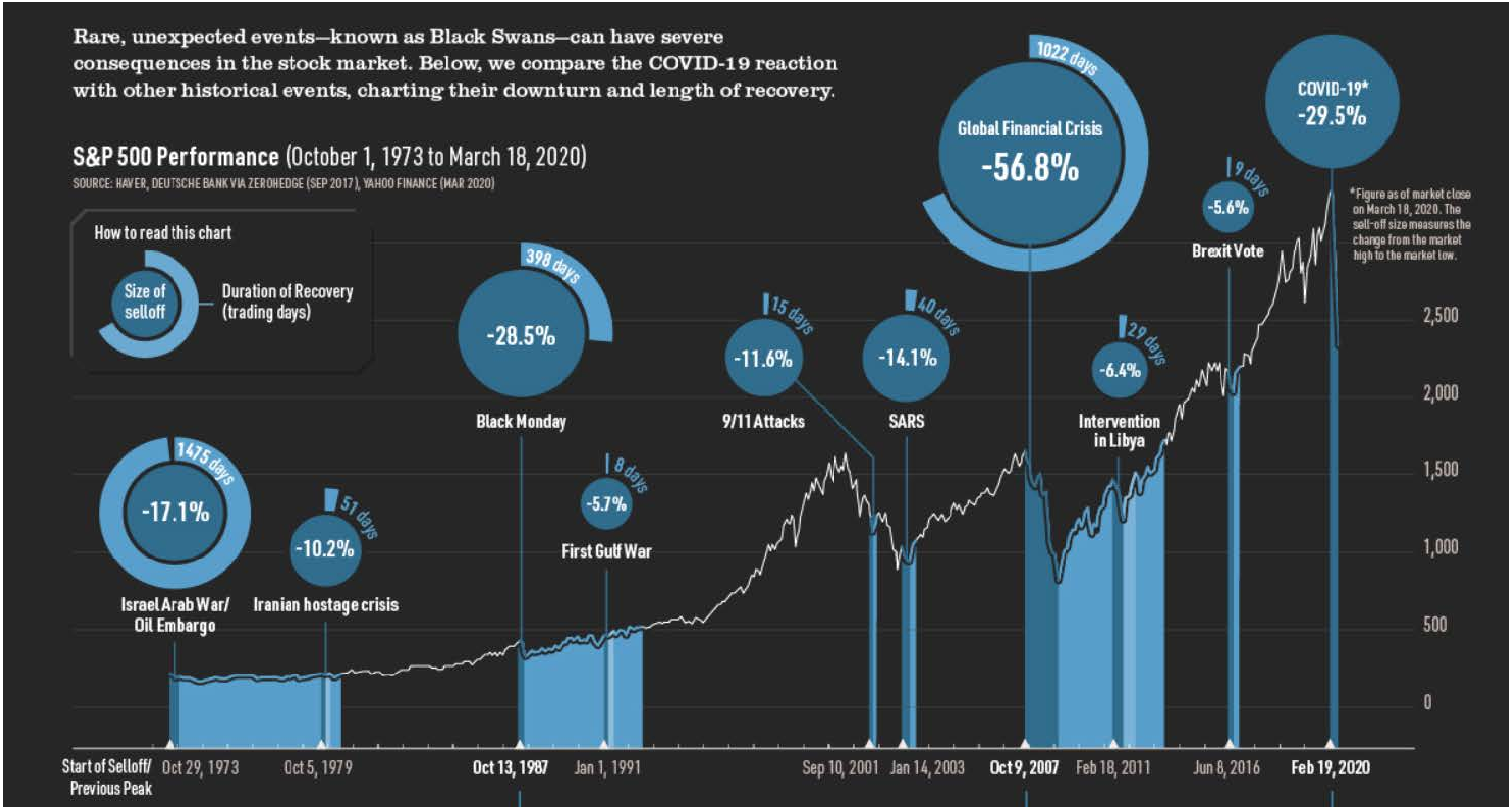
Infrastruktur

Real Estate

…

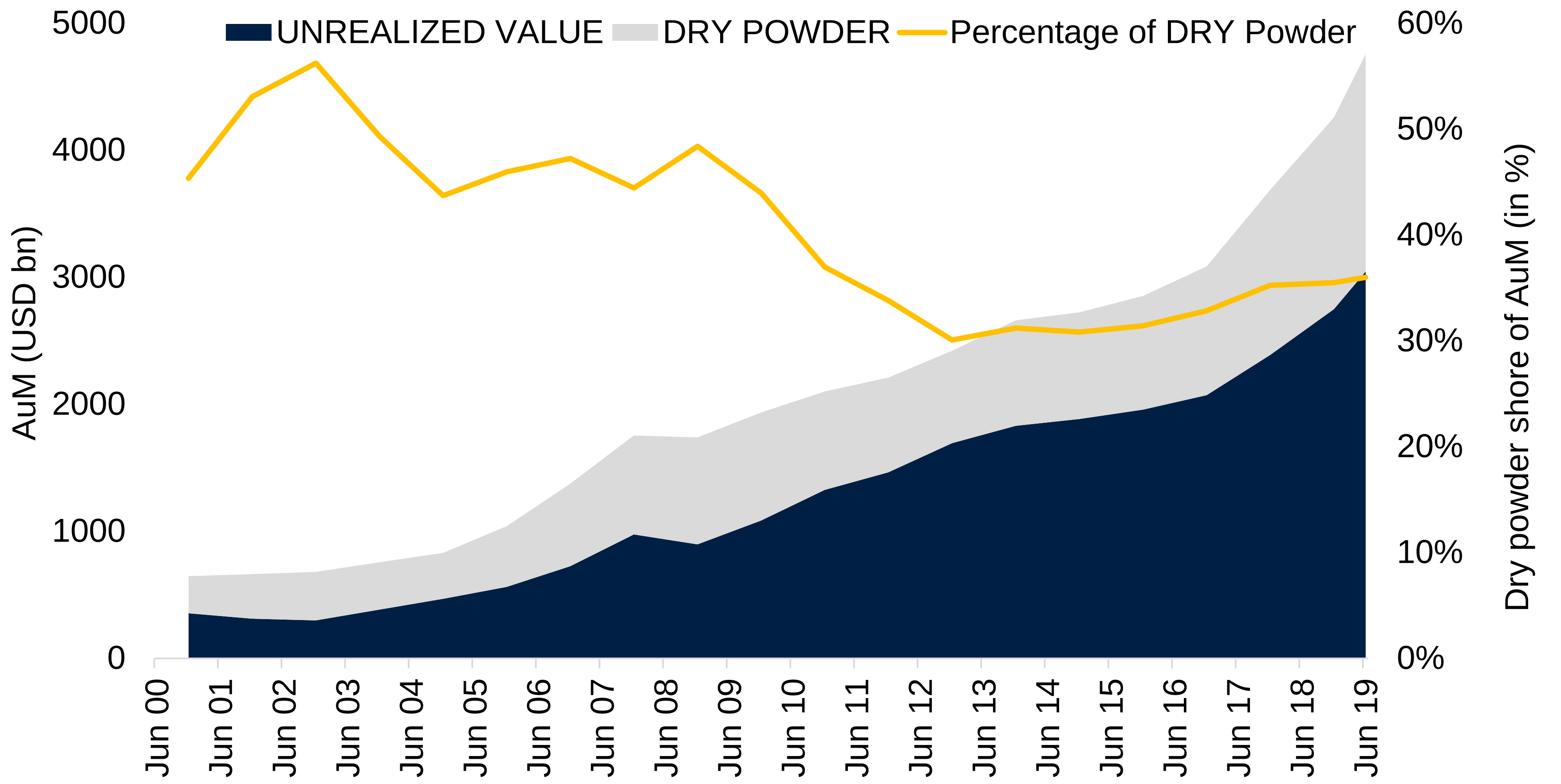
Die wirtschaftlichen Auswirkungen der Corona-Pandemie: Wie geht es weiter? Prof. Lars Feld, 22.4.20

Black Swan Events: Short-term crisis: Long-term opportunity



Source: Markets in a minute, visual capitalist

Development of Dry Powder over time



Source: Preqin Pro, BAI.

Quelle: Münstersche Zeitung

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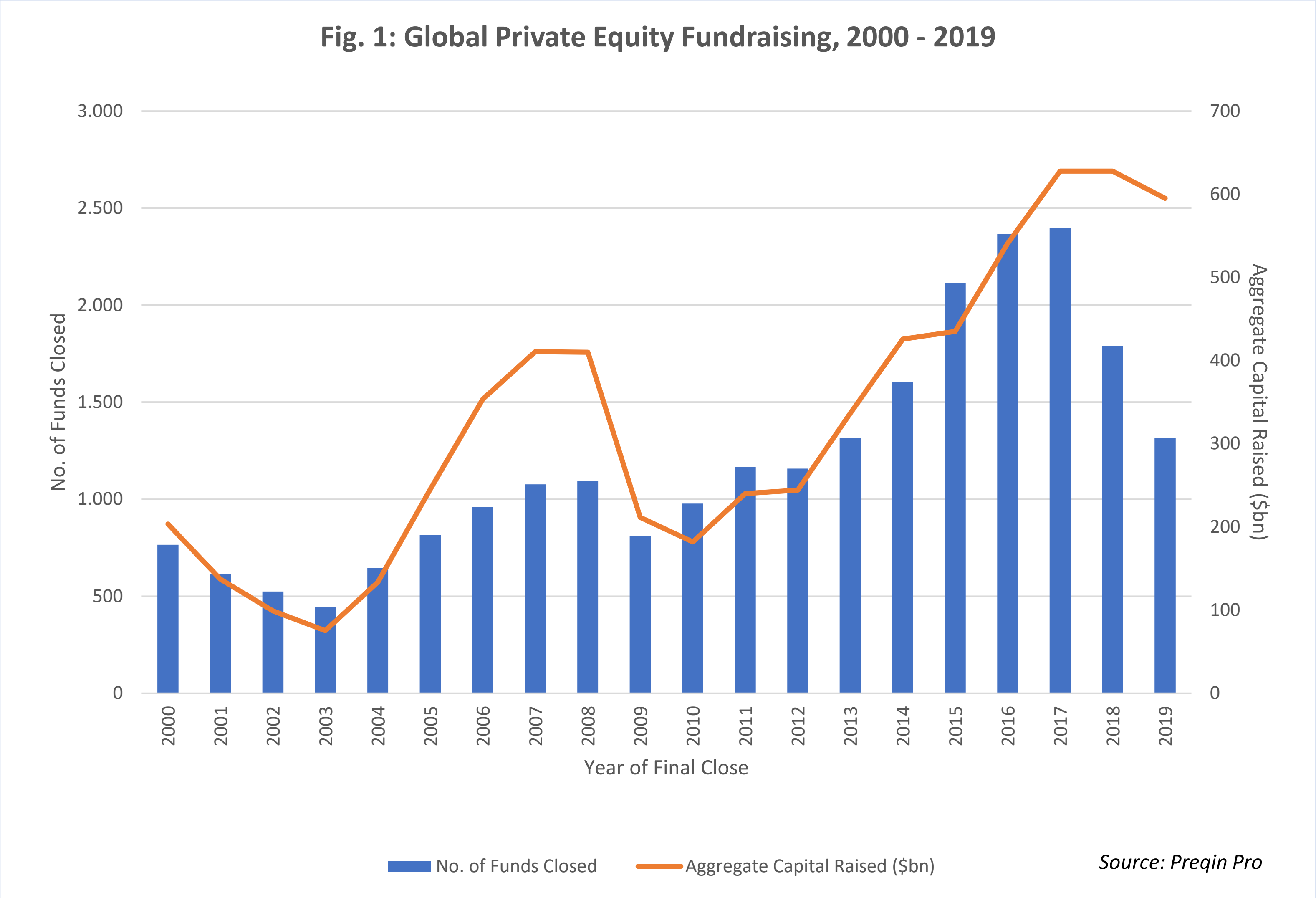
Fig. 1: Global Private Equity Fundraising, 2000 - 2019
3.000
2.500
2.000
1.500
1.000
500
0
700
600
500
400
300
200
100
0
No. of Funds Closed
Aggregate Capital Raised ($bn)
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018
2019
Year of Final Close
No. of Funds Closed
Aggregate Capital Raised ($bn)
Source: Preqin Pro

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Navigating the unchartered

How can private equity investors respond to the COVID-19 environment?

Nils Rode, Chief Investment Officer

March 2020

Base case scenario

- Several months of economic impact from lock-downs
- Stock market correction
- Global recession[1]

If the situation turns out to be less severe than assumed, everyone will express relief and will not regret, for having prepared for greater downside risks.

[1]Schroders economic forecast, March 19, 2020: «Coronavirus to spark severe global recession”
Source: Schroder Adveq, 2020.

Content

Expected developments for

01 Existing private equity investments overall and by strategy, region and industry

- Valuations
- Cash flows (contributions, distributions)
- Reserves for follow-on financings
- ESG considerations
- Monitoring and risk management questions to ask

02 Private equity allocations

03 New investment opportunities

04 Possible long term effects

Valuations

Expected developments

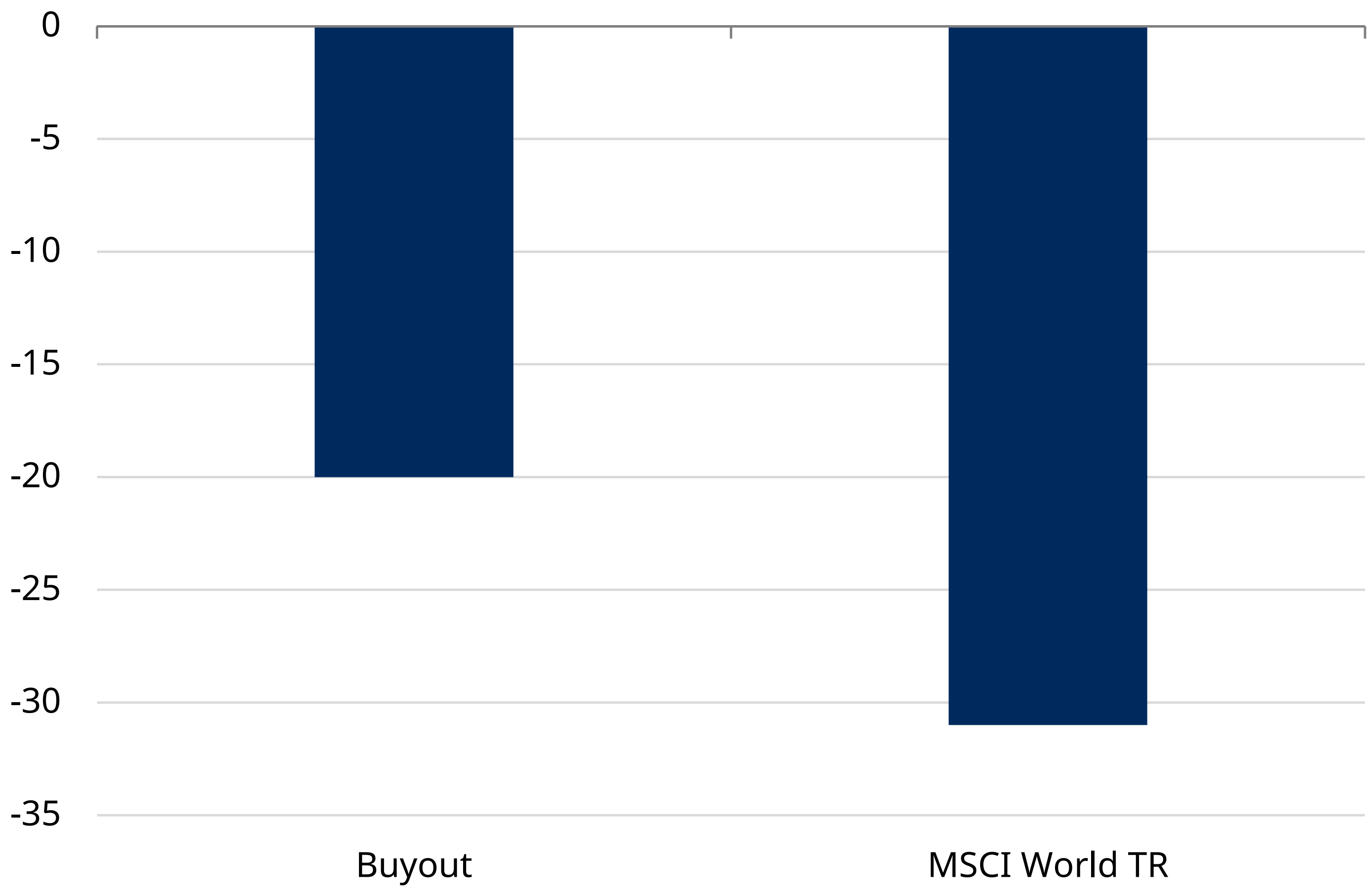
- Private equity to prove more resilient overall than stock markets
- Meaningful corrections for private equity between half and the full level of stock market corrections, depending on the strategy (e.g. 15–30% in case of a 30% stock market correction)
  - Highest correction (more than stock markets) for secondary focused funds that aggressively utilize fund-level leverage and third-party financing on underlying transactions
  - High correction for large buyouts and late stage growth (in line with public market sector equivalents)
  - Lower correction for small buyouts and early stage venture (about half of stock market corrections)
- Strong difference in valuation impact by industry
- Adjusted valuations only to become visible for Q1 2020 and Q2 2020 valuations (in May and August 2020) with the full valuation impact realized several quarters following the stock market trough

Source: Schroder Adveq, 2020.

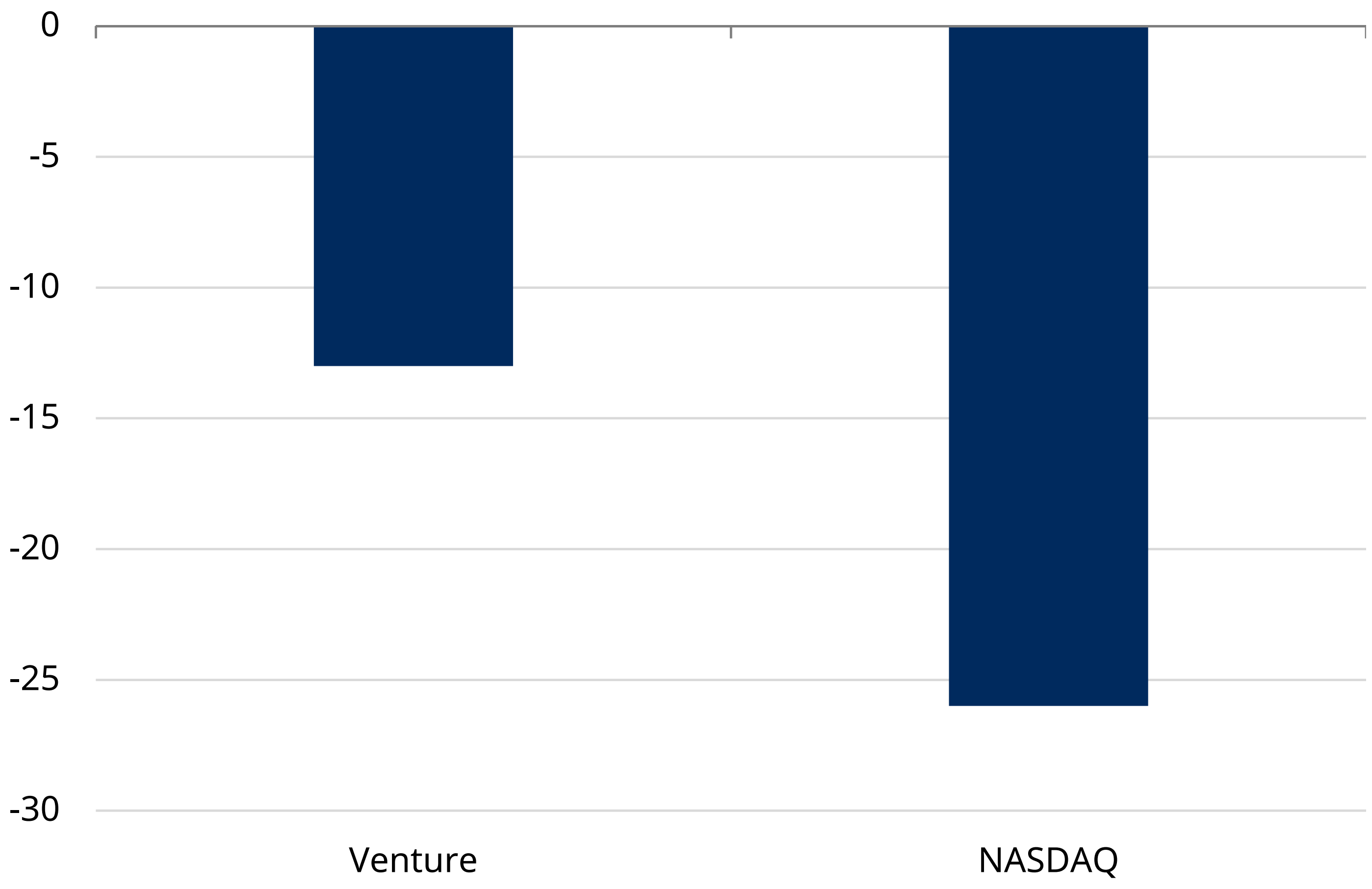
Private equity valuations are expected to correct less than stock markets for most private equity strategies

Maximum valuation correction in 2008–2009

Valuation correction buyout vs. listed equities (2008–09)



Valuation correction venture vs. listed equities (2008–09)

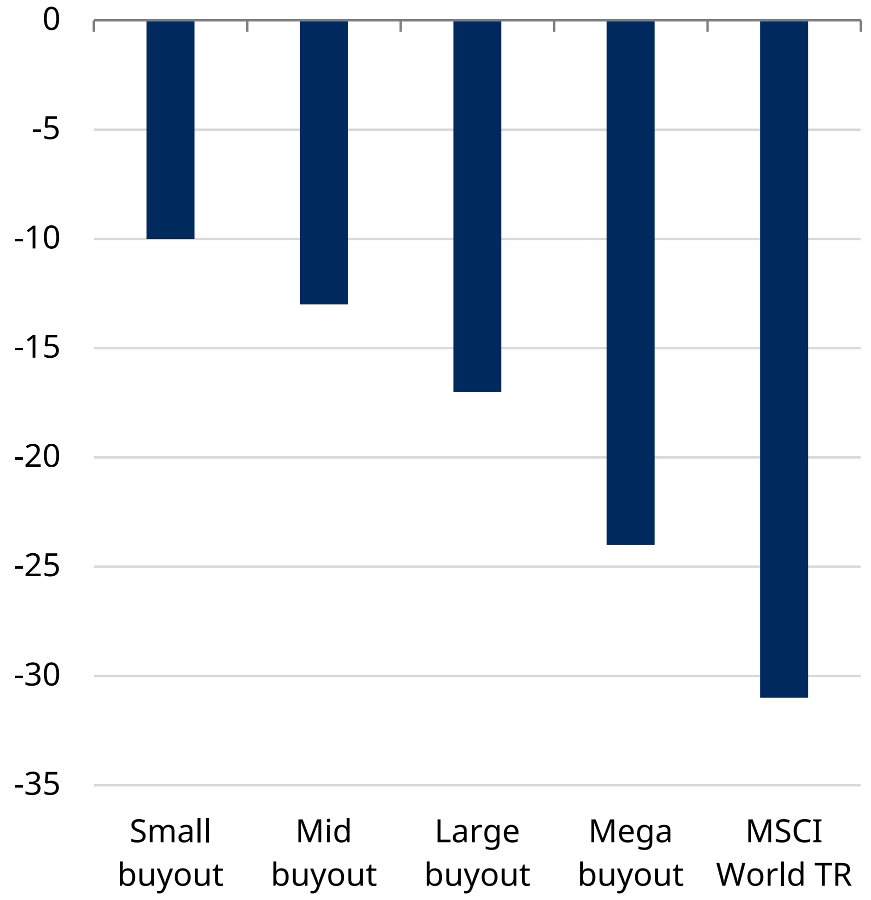


Source: Preqin, Schroder Adveq Maximum drawdown shown is maximum valuation correction for period of 09/2008 to 09/2009.

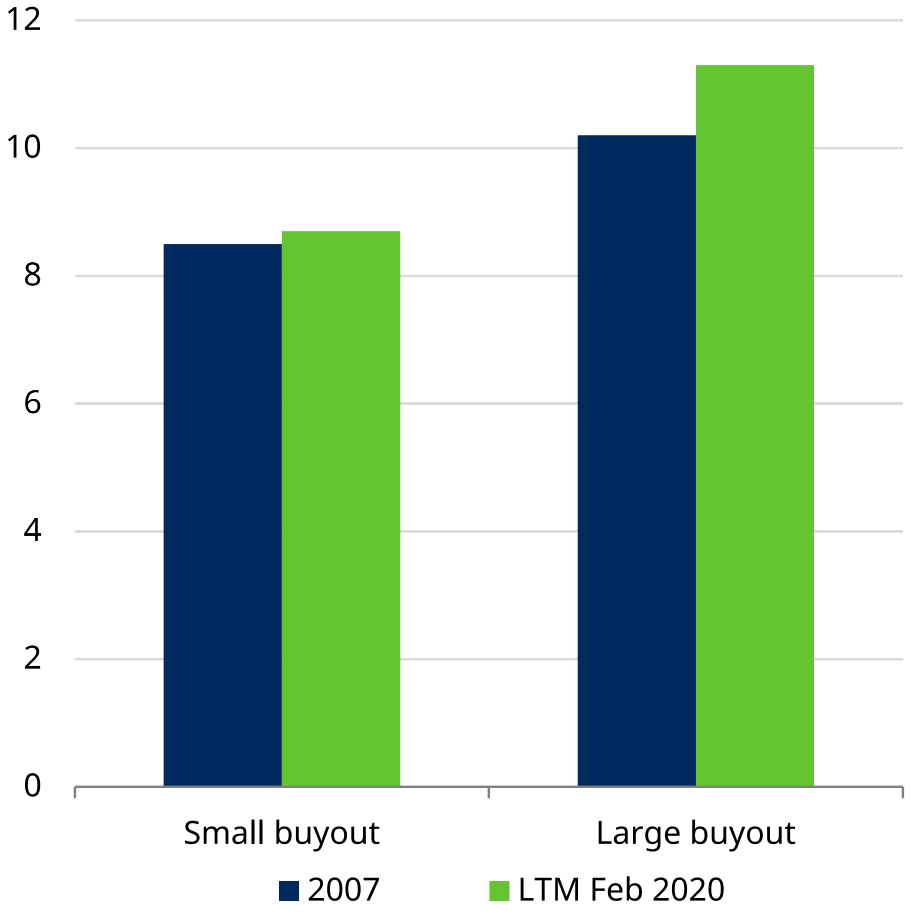
Valuation correction depending on size range

Valuation considerations for buyouts

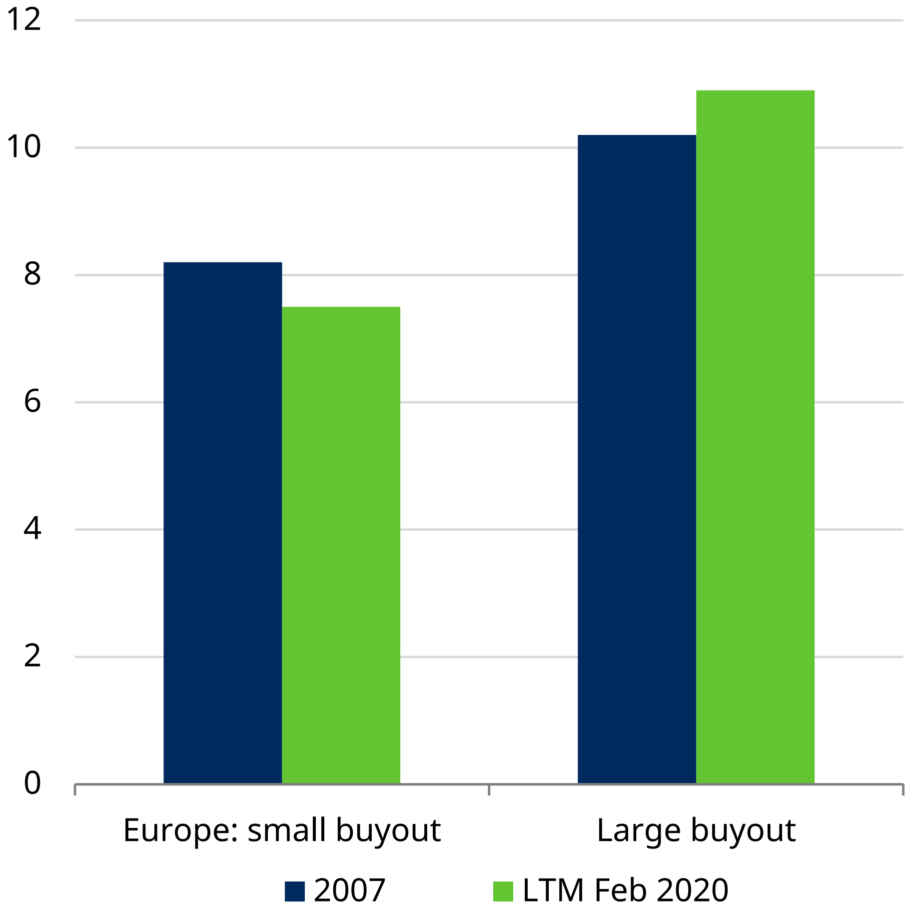
Valuation correction buyout vs. listed equities (2008/09)



Buyout valuations (EV/EBITDA multiples) – US



Buyout valuations (EV/EBITDA multiples) – Europe



Source: Preqin, Baird, S&P, Schroder Adveq 2020, Maximum drawdown shown is maximum valuation correction for period of 09/2008 to 09/2009.

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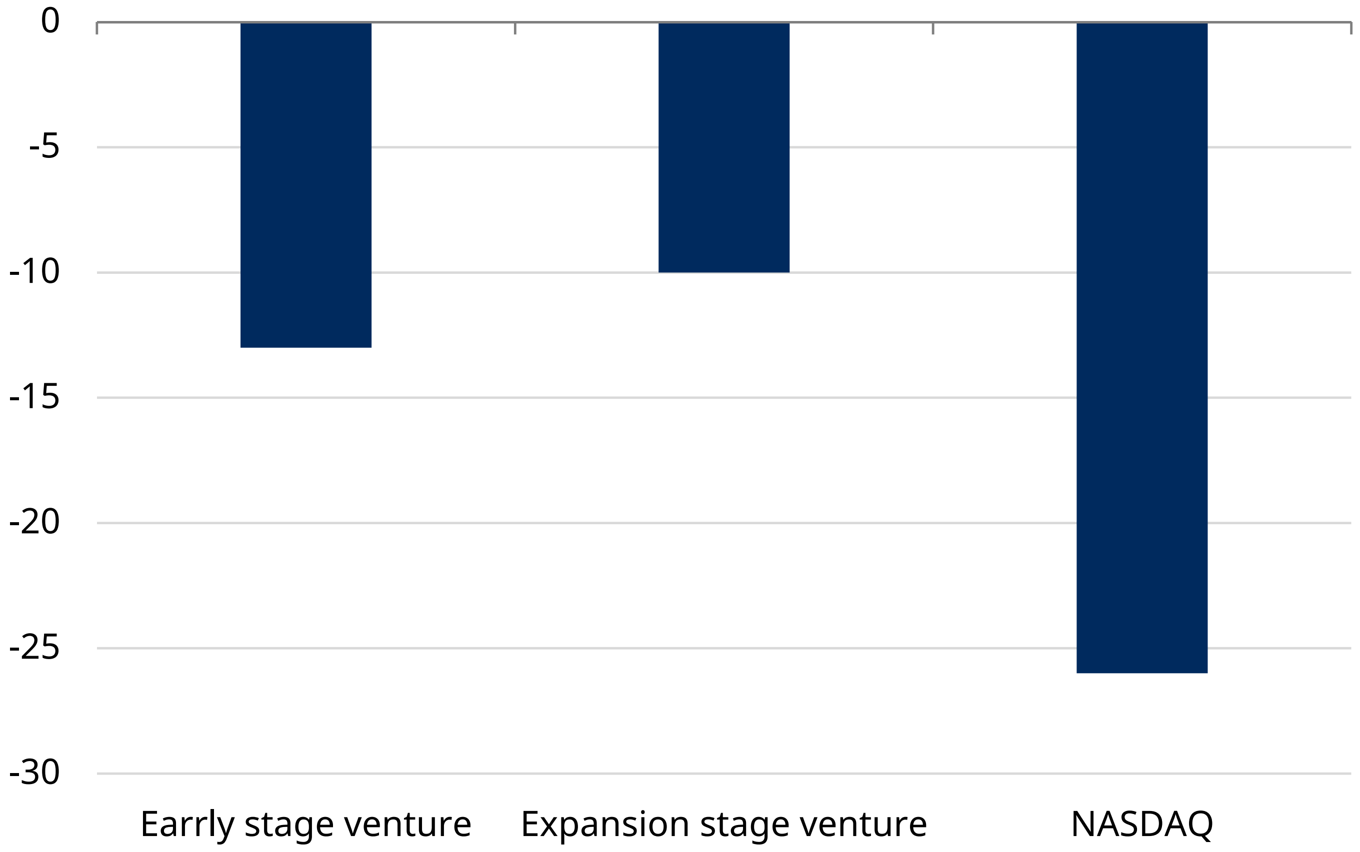
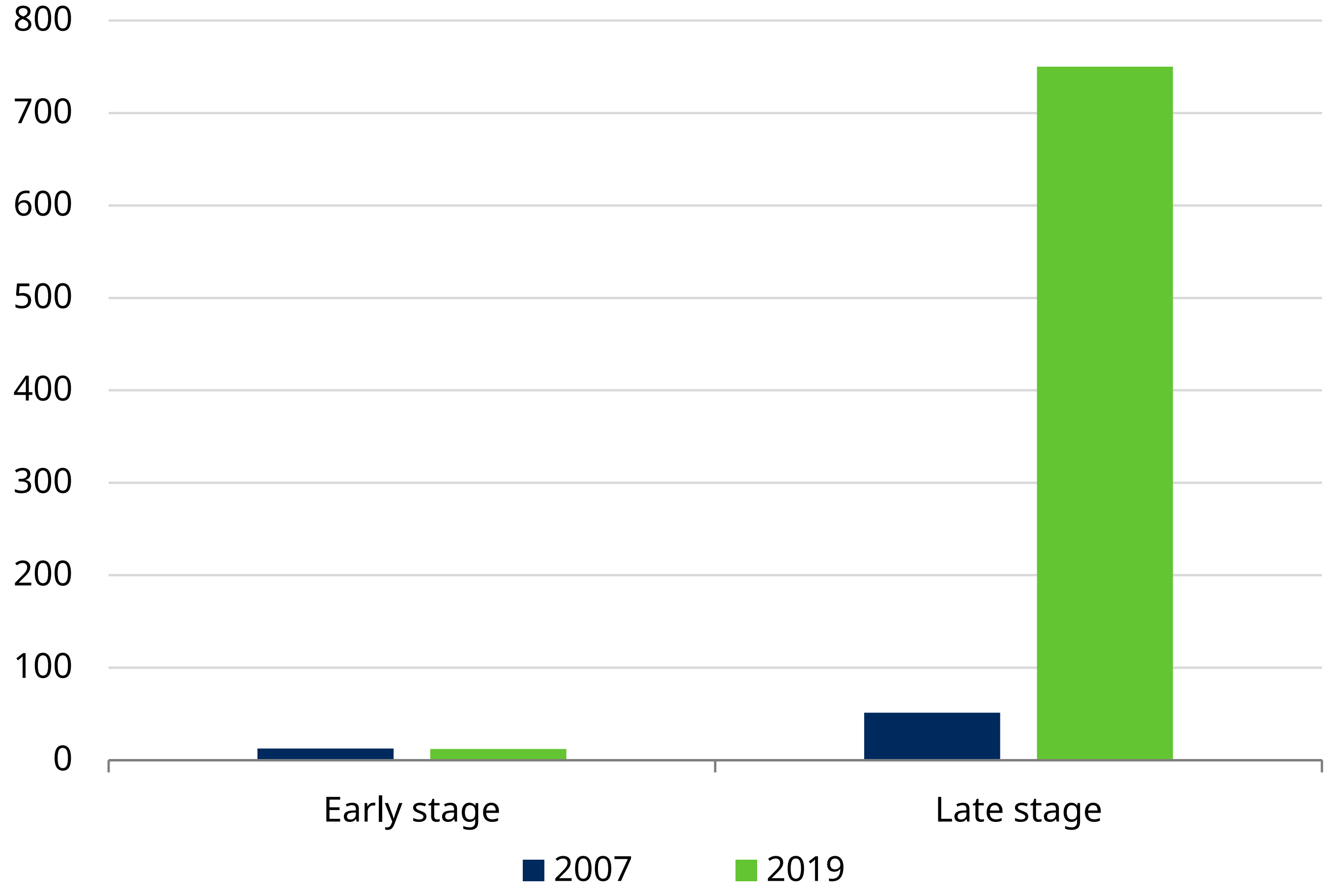
Early stage with limited, late stage/growth with strong expected valuation correction

Venture Capital valuation considerations

Valuation correction venture vs. listed equities (2008–09)



Venture valuations (medium pre-money)



Source: Preqin, VentureSource, Pitchbook, Schroder Adveq, 2020, Maximum drawdown shown is maximum valuation correction for period of 09/2008 to 09/2009.

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Valuation impact varies by industry

Economic impact from social distancing and government interventions

Industries that we expect to be most impacted

- Travel/hospitality/leisure
- Aviation
- Automotive / mobility
- Oil/gas
- Discretionary consumer goods
- Consumer and business lending

Industries that we expect to be least impacted

- Consumer staples
- Healthcare
- Online media/entertainment
- E-commerce
- Enterprise software

Source: Schroder Adveq, 2020.

Cash flows

Expected developments

Contributions

- Initial spike for rescue financing and paying down subscription credit facilities
- Slow-down of >50% in investment pace for new opportunities
- Higher slow-down for buyouts than for venture capital

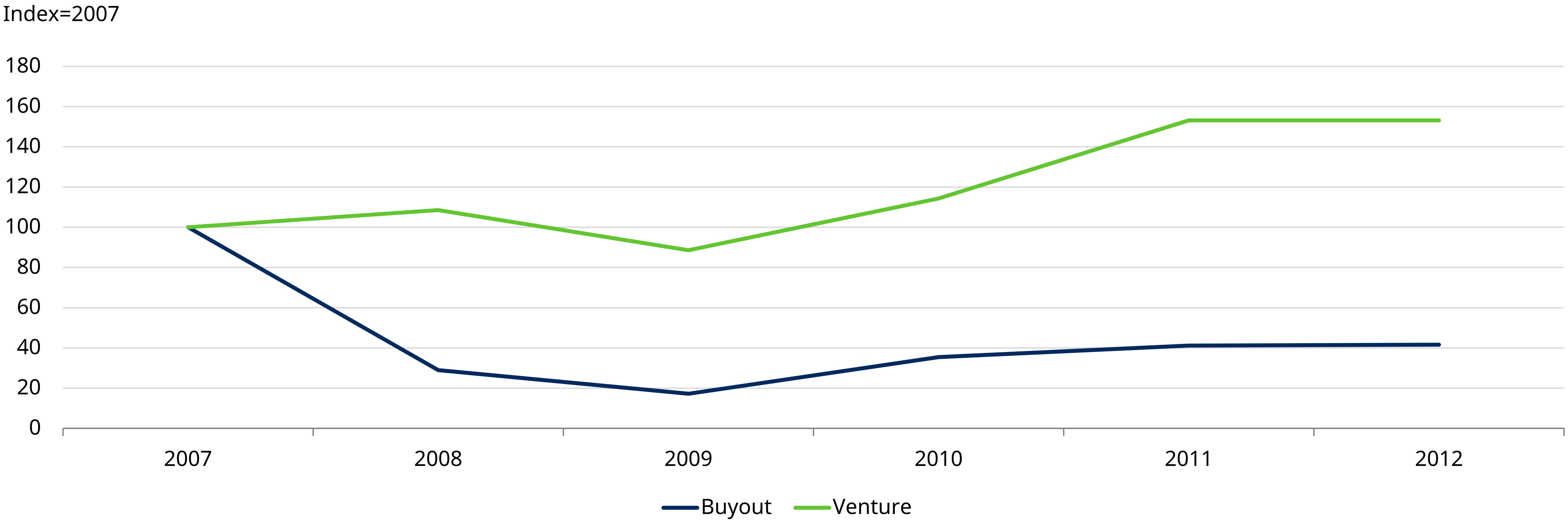
Distributions

- Exit window closed
- Distributions to come to a halt for several quarters

Source: Schroder Adveq, 2020.

Buyout/growth investment pace expected to go down significantly, early stage venture expected to be more stable

Deal volume during the 2008–09 crisis



Source: Preqin, Schroder Adveq, 2020.

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Reserves/follow-on financing

Expected developments

- Wave of top-up/annex funds
- Equity cures for some direct/co-investments
- Follow-on financings more complicated and with conflict potential due to prevalence of co-investments with different shareholders who might have different abilities to fund follow-on financings

Source: Schroder Adveq, 2020.

ESG considerations

Expected developments

- Environmental, social and governance (ESG) focus will rapidly shift from ‘E’ to ‘S’ and ‘G’
- Investors who are directly invested in funds and direct/co-investments will pay increasing attention to headline risks

Source: Schroder Adveq, 2020.

Monitoring and risk management priorities

Expected developments

- Focus on social distancing as a new risk dimension
- Emphasis on identifying companies with follow-on financing needs
- Increased focus on management of subscription credit facilities and other types of fund financing structures (that are much more prevalent today than in 2008–09)

Source: Schroder Adveq, 2020.

Monitoring and risk management questions to ask

Investors should proactively seek portfolio-specific updates related to COVID-19

A useful framework is to categorize all investments in four categories

	Company category	Description	Mitigation measures during crisis
1	‘Anti-fragile’ companies	Companies that benefit from the current situation	Growth acceleration
2	Robust companies	Companies that will demonstrate robustness with regard to revenues and profitability, but might experience a valuation decline driven by market comparables	Heightened risk management
3	Fragile companies	Companies that will experience some level of revenue and profitability impact, but have no or low financing risks	Cost reductions
4	Companies with permanent impairment risks	Companies that will require some type of additional financing to support their business during this situation	Cost reductions, additional financing measures

Source: Schroder Adveq, 2020.

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Private equity allocations

Expected developments

- Return of the ‘denominator effect’
- No good choices for investors who feel forced to react to denominator effect (secondary sales at steep discounts, LP defaults)
- Private equity allocations will benefit from environment with record low interest rates

Source: Schroder Adveq, 2020.

New opportunities

Expected developments

- Flight to quality/focus on established providers and fund managers
- Primaries to benefit from new valuation environment
- Opportunity to increase access to and allocation with exclusive fund managers
- Top-up/annex funds with attractive deal structuring
- Attractive secondary opportunities expected to emerge as early as second half of 2020
- Direct/co-investments are the most immediate opportunity with the need to apply additional selection filters

Source: Schroder Adveq, 2020.

Like with any major crisis, there will be long-term effects

Possible long-term effects of the current crisis

Issue surfacing in this crisis	Possible long term effect
– Certain private equity investments and investment structures with hidden or too much leverage	– More focus on look-through leverage and risk profiles of private equity investments
– Overleverage of certain large corporates	– Renewed focus on corporates' core business and need to raise capital leading to increased deal flow from corporate carve outs
– Global supply chain disruptions	– Better supply chain diversification – Government mandated de-globalization in certain areas
– Need for social distancing leading to experience with work from home	– More flexible work environments with more work from home
– Need for social distancing leading to more online transactions	– Permanent growth boost for online services and online commerce
– Healthcare supply shortages, lack of pandemic preparedness	– Increased demand for certain healthcare goods and services

**It is too early to fully assess the long term effects at this point in time.
The above is intended as some initial food for thought.**

Source: Schroder Adveq, 2020.

More information

- Schroder Adveq to release a publication on the topic of this webinar shortly
- Contact: nils.rode@schroderadveq.com

Source: Schroder Adveq, 2020.

Important information (1/2)

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	Gross value	Net value	Compound effect
1 Year	$5,500,000	$5,460,625	$39,375
3 Years	$6,655,000	$6,513,090	$141,910
5 Years	$8,052,550	$7,768,403	$284,147
10 Years	$12,968,712	$12,069,617	$899,095

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