PREQIN QUARTERLY UPDATE: PRIVATE EQUITY & VENTURE CAPITAL

Q1 2019

Fundraising
Funds in Market
Investors
Deals
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Dry Powder

FOREWORD

The private equity industry is preoccupied by a key question in 2019: which sectors will be worst affected by the expected equity market downturn? Fund managers and investors alike widely believe it is due within the next 12-24 months, so are positioning themselves accordingly – and their preparations are driving industry trends in Q1.

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For investors, the overall appeal of private equity has not diminished. Historically, the asset class has consistently outperformed public markets, even through previous financial crises. Beyond return generation, private equity investments offer diversification and inflation-hedging advantages which are particularly appealing to investors looking to protect their portfolios. However, in a period of uncertainty, investors are exercising caution, so capital is increasingly concentrating at the top end of the industry. This poses an ever more challenging landscape for smaller managers trying to secure funding.

On the deal-making side, it is a different story: both buyout and venture capital saw record levels of deal-making in 2018, and much of that momentum has carried over to the first part of this year. Dry powder has continued to accumulate, and yet fund managers are clearly able to put capital to work, despite concerns about high asset pricing and competition for deals. The pressure that competition puts on future returns is undeniable and, though it may be that the days of double-digit performance for the industry are over, many fund managers and investors still see private equity as a strong performer in the months and years to come.

CONTENTS

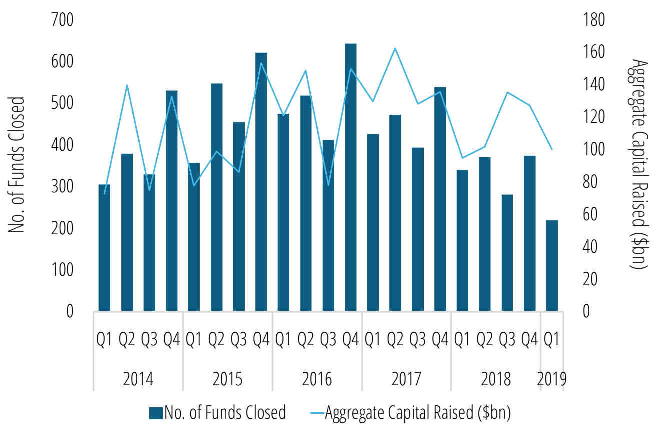
FUNDRAISING

Historically, the first quarter of the year is a quieter period for fundraising; this was certainly the case for Q1 2019, as both the number of funds closed and the total capital raised declined from Q4 2018 (Fig. 1).

Appetite for the asset class remains strong, though, despite concerns about a potential market downturn: 219 funds raised a combined $100bn in Q1, in line with the $95bn secured in Q1 2018. Where figures differ, though, is the number of funds closed in each period, with 340 funds closed in Q1 2018. Capital is becoming more concentrated among a small number of large funds, and Q1 2019 is on course to mark a five-year low in the quarterly number of funds closed.

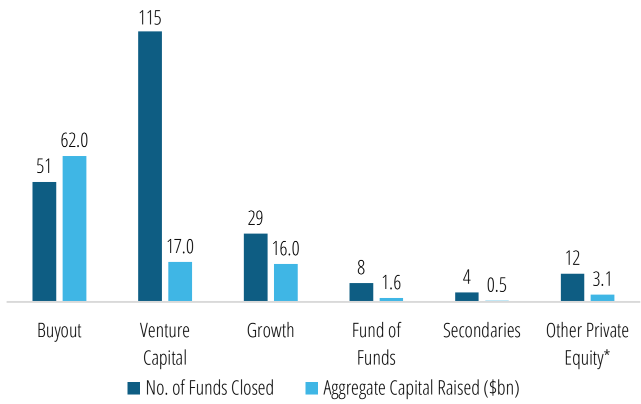
While Asia has come to the forefront of the industry in recent years, fundraising activity seems to be refocusing on North America, and vehicles targeting the region marked their second highest Q1 fundraising total (133 funds secured $63bn, Fig. 3). Conversely, Europe-focused activity struggled to rebound from its fundraising lull, with Q1 2019 recording the lowest level of activity in an opening quarter since 2015.

Fig. 1: Global Quarterly Private Equity Fundraising, Q1 2014 - Q1 2019



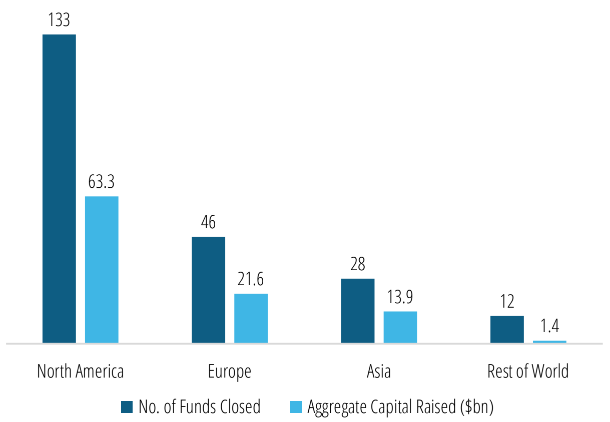
Source: Preqin Pro

Fig. 2: Private Equity Fundraising in Q1 2019 by Fund Type



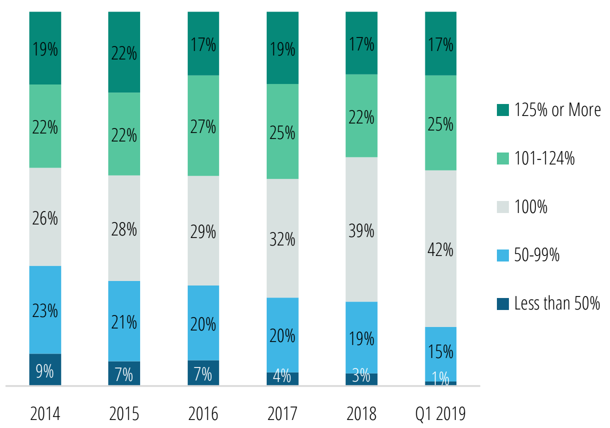
Source: Preqin Pro

Fig. 3: Private Equity Fundraising in Q1 2019 by Primary Geographic Focus



Source: Preqin Pro

Fig. 4: Private Equity Funds Closed by Proportion of Target Size Achieved, 2014 - Q1 2019



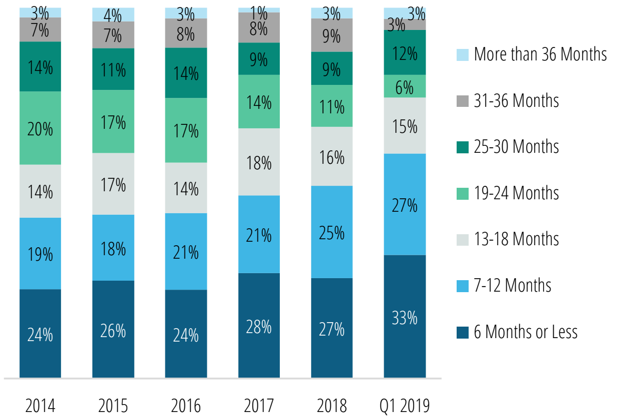
Source: Preqin Pro

"Other Private Equity' includes balanced, co-investment, co-investment multi-manager, direct secondaries and turnaround funds.

Among Asia-focused funds this downward trend is even more pronounced: 28 funds secured $14bn in Q1 2019, which represents the fifth consecutive quarterly decline in the number of funds closed, as well as the second-lowest quarterly capital total in the past five years. This is not necessarily indicative of a slowing market overall – there are a large number of Asia-focused funds currently in market, many of which have already secured significant capital through interim closes. It may suggest that, in a crowded marketplace, fund managers are finding it more difficult to attract sufficient capital to complete their fundraising process.

While the number of funds closed globally was low, those funds able to close in Q1 2019 generally did so quickly and successfully. The proportion of funds failing to reach their targets has fallen year on year to reach a new low of just 16% in Q1 (Fig. 4). At the same time, six out of 10 funds closed had been in market for 12 months or less, a significant jump from previous years. This further points to the emergence of a two-tiered fundraising market, wherein experienced fund managers are routinely oversubscribed and so can raise large sums of capital in a quick fundraising process.

Fig. 5: Average Time Spent in Market by Private Equity Funds Closed, 2014 - Q1 2019



Source: Preqin Pro

Fig. 6: Largest Private Equity Funds Closed in Q1 2019

Fund	Firm	Fund Size (mn)	Final Close Date	Fund Type	Geographic Focus
Thoma Bravo Fund XIII	Thoma Bravo	12,600 USD	Jan-19	Buyout	North America
Genstar Capital Partners IX	Genstar Capital Partners	7,000 USD	Feb-19	Buyout	US
Summit Partners Growth Equity Fund X	Summit Partners	4,900 USD	Mar-19	Growth	Europe, North America
TPG Asia VII	TPG	4,600 USD	Feb-19	Buyout	Asia, Australasia
Astorg VII	Astorg Partners	4,000 EUR	Jan-19	Buyout	Europe

Source: Preqin Pro

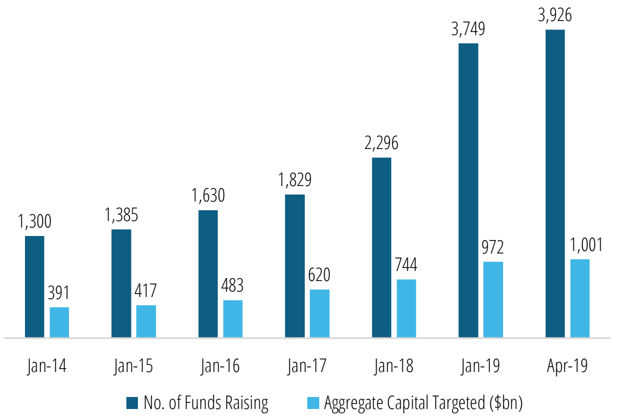
FUNDS IN MARKET

With 3,926 funds seeking an aggregate $1.0tn at the start of Q2 2019, the private equity fundraising market remains highly competitive (Fig. 7). This creates a very challenging landscape for funds seeking capital, but firms are still successfully managing to attract investment in significant quantities. Almost 2,500 of the funds currently in market have held at least one interim close, securing a total of $361bn.

A number of mega funds are driving fundraising activity by holding drawn-out fundraising processes while simultaneously beginning to make deals. Among them is SoftBank Vision Fund, which has raised over $90bn through interim closes and a handful of quasi-governmental China-based funds. This has distorted the fundraising market: 4% of funds on the road are targeting $1bn or more, and these vehicles account for almost 70% of all capital sought. The five largest funds alone are collectively seeking almost a quarter of a trillion dollars (Fig. 9).

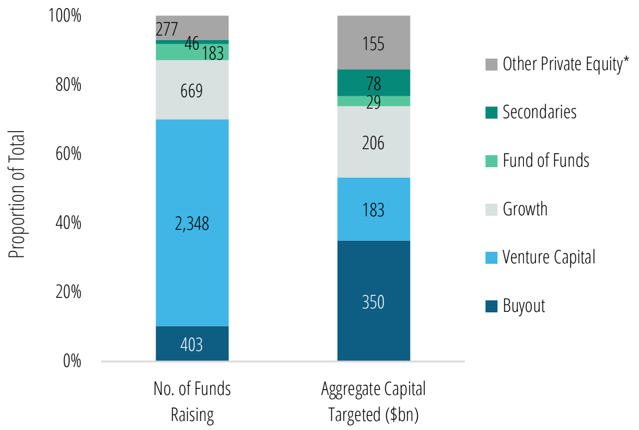
North America and Asia continue to vie for position as the most active fundraising market, with more than 1,500 funds focused on each region currently seeking investment. Europe, by contrast, has fewer than 500 funds in market, suggesting that fund managers see limited opportunity in the region. By a large margin, North America-focused funds are targeting the greatest amount of capital; the region has and will continue to attract interest because of the maturity of its private equity & venture capital market and the higher asset valuations within it.

Fig. 7: Private Equity Funds in Market over Time, 2014 - 2019



Source: Preqin Pro

Fig. 8: Private Equity Funds in Market by Fund Type



Source: Preqin Pro. Data as at April 2019

Fig. 9: Largest Private Equity Funds in Market

Fund	Firm	Target Size (mn)	Status	Fund Type	Geographic Focus
SoftBank Vision Fund	SB Investment Advisers	100,000 USD	Second Close	Hybrid	Global
China Structural Reform Fund	CCT Fund Management	350,000 CNY	First Close	Growth	China
China Integrated Circuit Industry Investment Fund II	SINO-IC Capital	200,000 CNY	Raising	Growth	China
ASF VIII	Ardian	18,000 USD	First Close	Secondaries	Europe, North America
Vista Equity Partners Fund VII	Vista Equity Partners	16,000 USD	First Close	Buyout	North America

Source: Preqin Pro. Data as at April 2019

**'Other Private Equity' includes balanced, co-investment, co-invest multi-manager, direct secondaries and turnaround funds.*

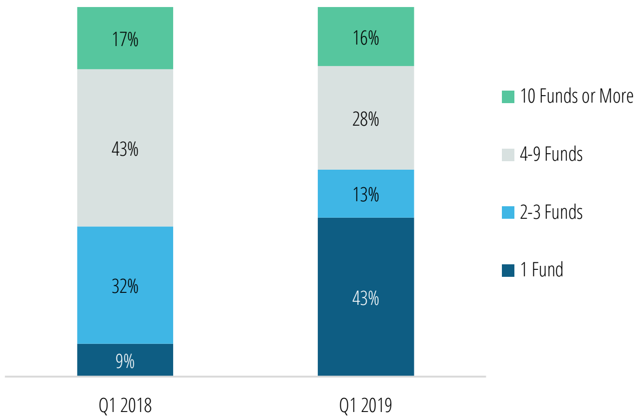
INVESTORS

During the first quarter of 2019, investors issued 233 new private equity fund searches and mandates. Over half (56%) of these investors expect to make up to three new fund commitments in the coming 12 months, and 28% are planning 4-9 commitments (Fig. 10). Although a comparison with mandates issued this time last year shows that investors are generally targeting fewer commitments, a noteworthy 16% of investors are planning 10 or more new investments in 2019. In terms of capital outlay, 20% of investors expect to commit at least $300mn in fresh capital to private equity in the next 12 months (Fig. 11), indicating that significant sums of capital will enter the asset class in the near future.

Buyout funds remain the most sought-after strategy among private equity investors, with 69% expecting to commit to these funds in the year ahead (Fig. 12). Appetite for venture capital funds has decreased compared to Q1 2018 (45% vs. 52% respectively), while the proportion of investors targeting growth funds has increased from 49% to 52%.

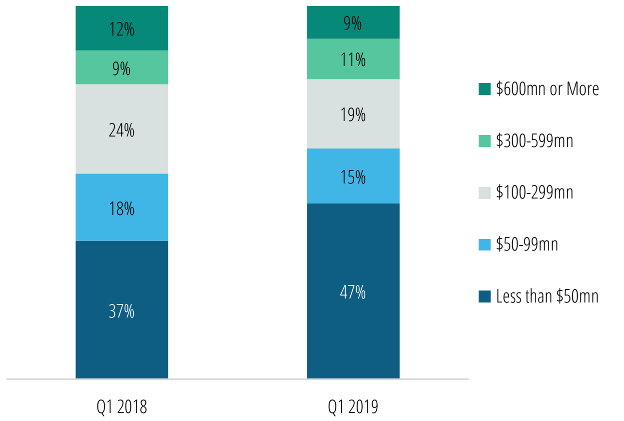
The largest proportion (57%) of mandates issued by investors target Europe-focused private equity funds, up from 51% at the start of 2018 (Fig. 13). Forty-six percent of investors are planning to commit to North America-focused funds, while 19% will target the Asia-Pacific region, down from 28% in Q1 2018.

Fig. 10: Number of Private Equity Funds Investors Plan to Commit to over the Next 12 Months, Q1 2018 vs. Q1 2019



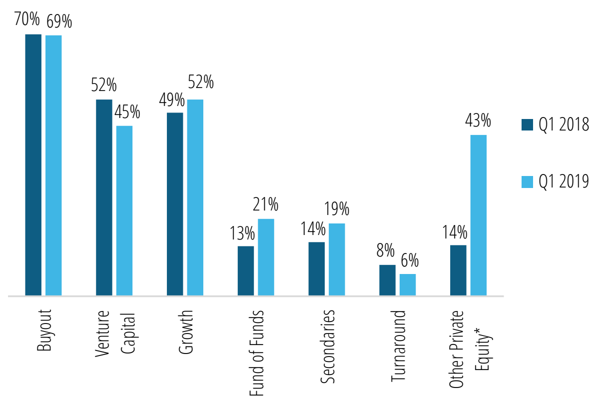
Source: Preqin Pro

Fig. 11: Amount of Fresh Capital Investors Plan to Commit to Private Equity Funds over the Next 12 Months, Q1 2018 vs. Q1 2019



Source: Preqin Pro

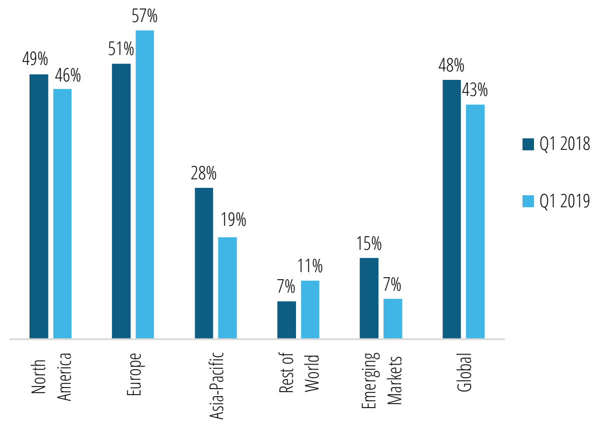
Fig. 12: Strategies Targeted by Private Equity Investors over the Next 12 Months, Q1 2018 vs. Q1 2019



Source: Preqin Pro

*'Other Private Equity' includes balanced, co-investment, co-invest multi-manager, direct secondaries and turnaround funds.

Fig. 13: Regions Targeted by Private Equity Investors over the Next 12 Months, Q1 2018 vs. Q1 2019



Source: Preqin Pro

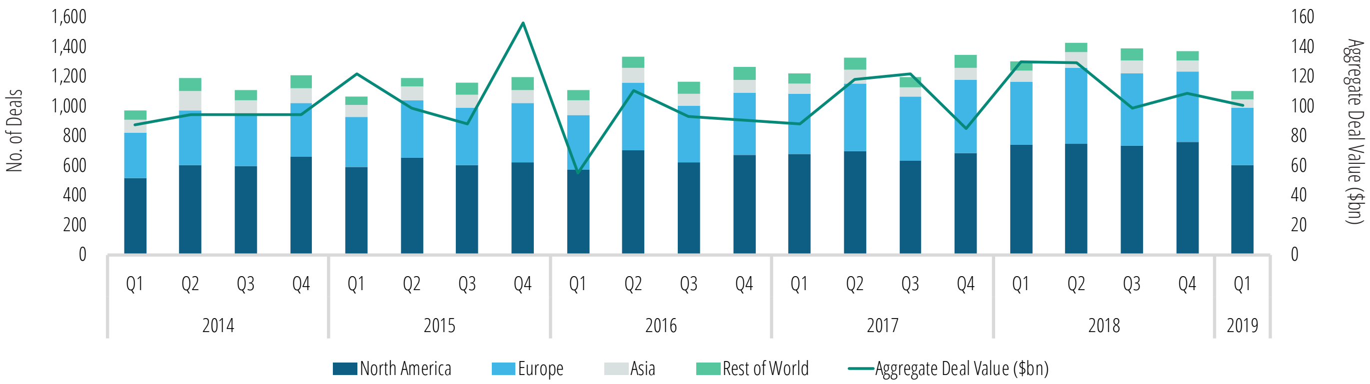
BUYOUT DEALS

2018 was a banner year for private equity-backed buyout deals, recording two of the three highest ever quarterly deal values and the top three quarters in terms of the number of deals announced (Fig. 14). The opening quarter of 2019 has not maintained this momentum: 1,100 buyout deals were announced globally, worth a combined $101bn. This total value exceeds is some way off the $130bn recorded in Q1 2018, though the number of deals has stayed on par with Q1 2016 (1,111).

The slowdown from Q1 2018 was primarily driven by a 65% fall in the value of Europe-based deals from $53bn to just $19bn (Fig. 15). Although aggregate deal value in the region had been climbing in 2016 and 2017, Q1 2018 marked a peak, and deal value has since declined back to 2016 levels. It is likely that many fund managers are waiting to see the terms of the UK's exit from the European Union before investing. The number and value of deals in both North America and Asia also fell – although by smaller margins – suggesting that the twin pressures of record amounts of available capital and high competition for deals may be primarily responsible. Faced with high valuations, managers are electing to wait rather than overpaying for acquisitions.

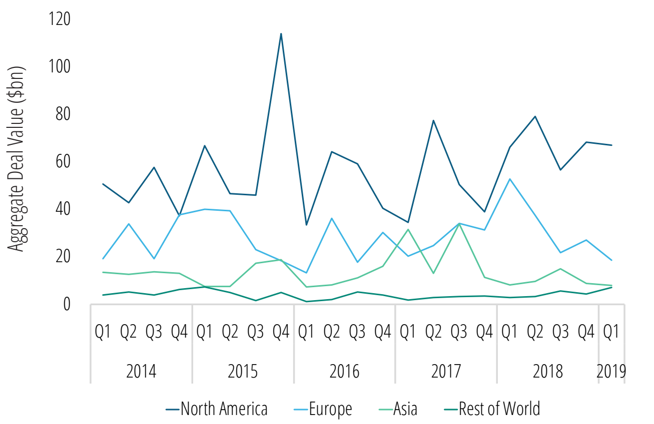
Challenging deal-making conditions often make for a favourable exit environment, but the number of buyout exits announced declined in Q1 2019, largely due to a 27% fall in the number of trade sales from Q4 2018 (Fig. 16). The total value of exits was also considerably lower at $67bn the previous quarter compared with $37bn in Q1 2019 – in fact, the quarter is on course to mark a five-year low in both the number and total value of buyout-backed exits.

Fig. 14: Private Equity-Backed Buyout Deals by Region, Q1 2014 - Q1 2019



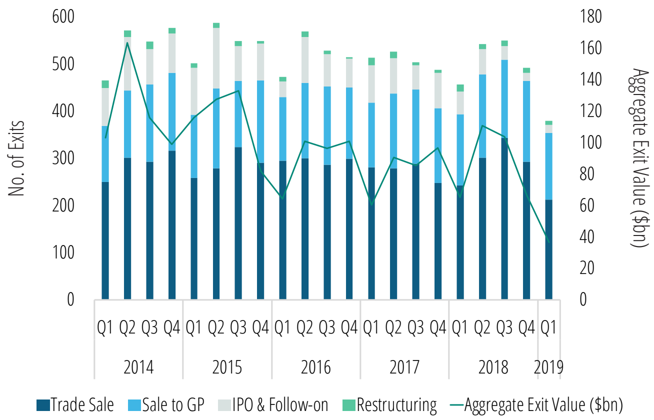
Source: Preqin Pro

Fig. 15: Aggregate Value of Private Equity-Backed Buyout Deals by Region, Q1 2014 - Q1 2019



Source: Preqin Pro

Fig. 16: Quarterly Private Equity-Backed Buyout Exits by Type, Q1 2014 - Q1 2019



Source: Preqin Pro

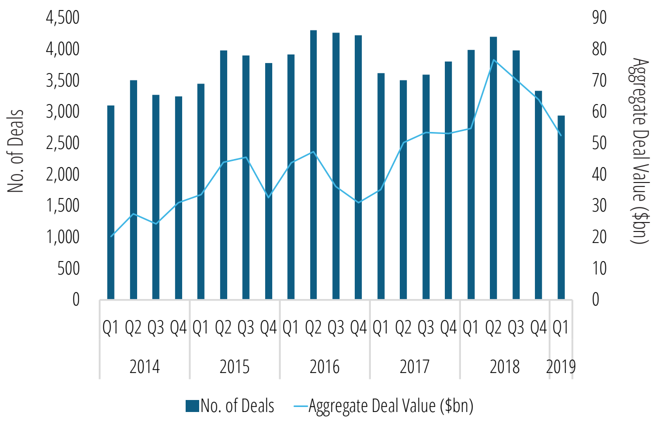
VENTURE CAPITAL DEALS

The opening quarter of 2019 did not match the records set in Q1 2018, which saw all-time highs for both the number and value of deals announced in an opening quarter (Fig. 17). However, while the 2,944 deals in Q1 2019 was some way off the 3,988 recorded in Q1 2018, deal values were on par – $52bn compared to $55bn respectively. It seems the deal-making boom has yet to lose momentum.

The role of Asia – and particularly China – in the venture capital deals boom is the hot topic of the quarter, and yet North America is also seeing record levels of activity. Q1 2019 represents the third consecutive record high in quarterly deal value for North America, whereas deal value in Greater China declined for the third consecutive quarter (Fig. 18). The two regions share responsibility for the slowdown in the number of deals announced; though all regions saw a decline, the number of deals in Greater China and North America fell by 46% and 21% respectively compared to Q1 2018.

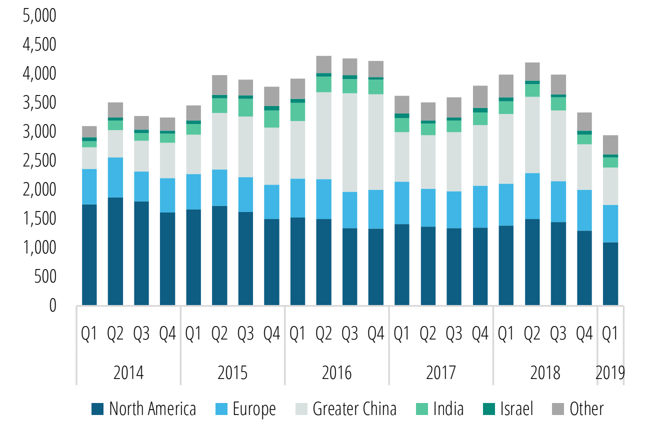
Venture capital exit activity has continued its protracted decline despite positive industry-wide deal-making trends. The number of exits has fallen across almost all types over the past five years, with only sales to GPs gaining any momentum (Fig. 20). The total value of venture capital exits has spiked in recent quarters, driven by the exit activity of a small number of large companies, but developing exit strategies for venture capital-backed companies is becoming increasingly challenging overall.

Fig. 17: Quarterly Venture Capital Deals*, Q1 2014 - Q1 2019



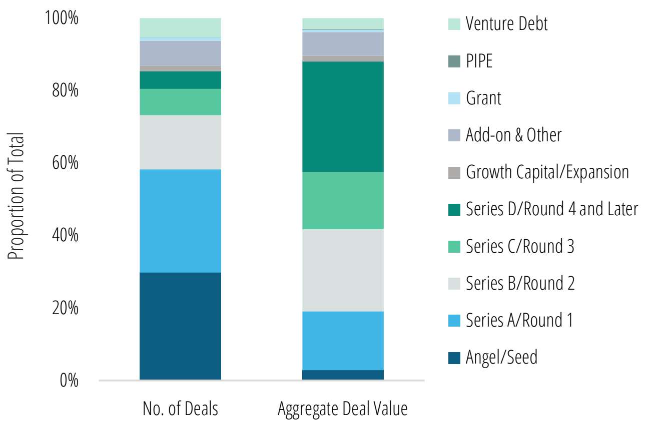
Source: Preqin Pro

Fig. 18: Number of Venture Capital Deals* by Region, Q1 2014 - Q1 2019



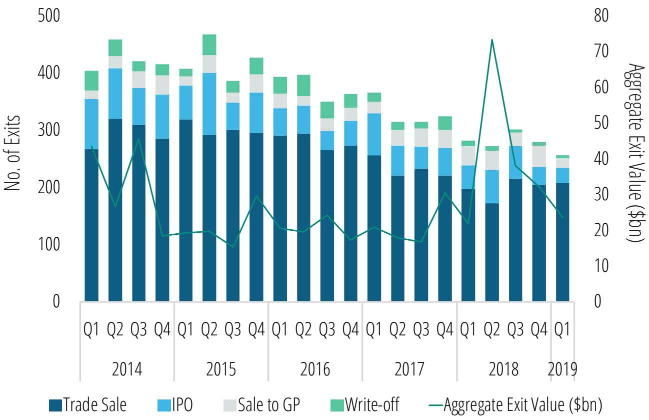
Source: Preqin Pro

Fig. 19: Venture Capital Deals in Q1 2019 by Stage



Source: Preqin Pro

Fig. 20: Quarterly Venture Capital Exits by Type, Q1 2014 - Q1 2019



Source: Preqin Pro

*Figures exclude add-ons, mergers, grants, secondary stock purchases and venture debt.

PERFORMANCE & DRY POWDER

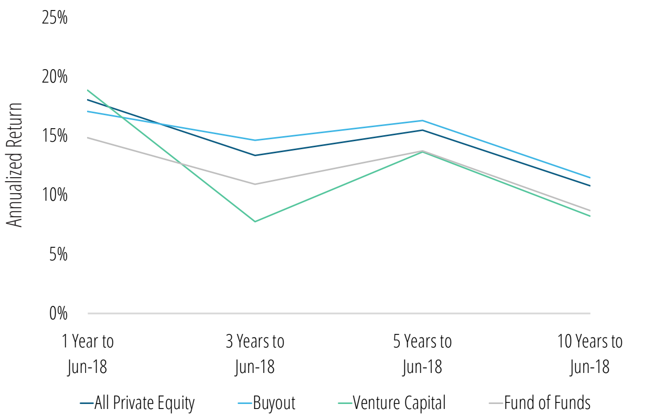
Private equity funds have delivered strong, double-digit returns over the one-, three-, five- and 10-year periods to June 2018 (Fig. 21). Buyout funds have displayed the highest annualized IRRs over three (+14.6%), five (+16.3%) and 10 (+11.5%) years, while venture capital funds have delivered the highest return over one year (+18.9%).

Fig. 22 clearly demonstrates the effects of the Global Financial Crisis on private equity returns: vintage 2005 and 2006 funds have delivered a median net IRR of 8.0% and 8.3% respectively compared to returns in the low- to mid-teens for later vintage years.

Following six consecutive years of positive net cash flow, capital calls exceeded distributions in 2017 by $5.0bn, pushing cash flow into negative territory once again (Fig. 23). In the first half of 2018 (the latest data available), cash flow returned to positive after a notable $262bn was distributed against $195bn called up.

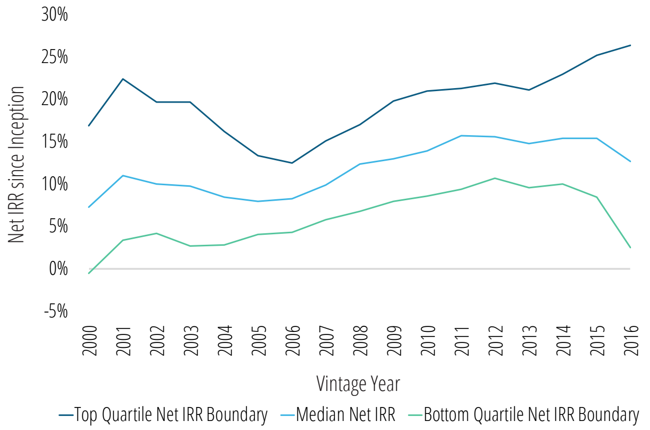
Industry dry powder continues to reach new records, with $1.26tn held in private equity funds as of March 2019 (Fig. 24). Buyout funds account for the majority (59%) of this dry powder, while venture capital and growth funds hold 17% and 5% of the total respectively.

Fig. 21: Private Equity: Horizon IRRs by Fund Type



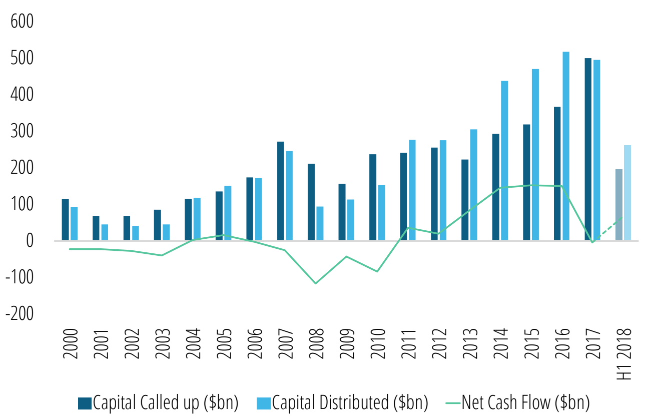
Source: Preqin Pro

Fig. 22: Private Equity: Median Net IRRs and Quartile Boundaries by Vintage Year



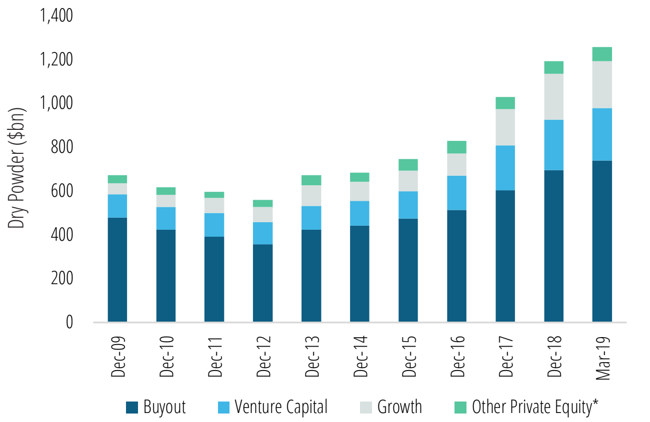
Source: Preqin Pro. Most Up-to-Date Data

Fig. 23: Private Equity: Annual Capital Called up, Distributed and Net Cash Flow, 2000 - H1 2018



Source: Preqin Pro

Fig. 24: Private Equity: Dry Powder by Fund Type, 2009 - 2019



Source: Preqin Pro

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