2025

Global Private Equity Outlook

Dechert LLP

Mergermarket

Contents

Methodology

In July 2024, *Mergermarket*, on behalf of Dechert LLP, surveyed 100 senior-level executives at PE firms based in North America (45%), EMEA (35%) and Asia-Pacific (20%). In order to qualify for inclusion, the firms all needed to have US$1 billion or more in assets under management (AUM) and respondents could not be first-time fund managers. The survey included a combination of qualitative and quantitative questions, and all interviews were conducted over the telephone by appointment. Results were analyzed and collated by *Mergermarket*, and all responses are anonymized and presented in aggregate.

Foreword

Welcome to the seventh edition of Dechert's *Global Private Equity Outlook*, our comprehensive annual report on the global private equity (PE) sector. We are delighted to once again present our view of where the PE market stands today – and the challenges and opportunities that lie ahead.

Our research, produced in conjunction with *Mergermarket*, provides compelling insights into an industry that has been through a period of seismic change. After 15 years of ultra-low interest rates, the PE sector has had to adjust to more normal borrowing costs over the last three years – and to endure a period of almost constant geopolitical volatility, economic turmoil and industry upheaval.

Against such a backdrop, our research provides crucial context. It represents an opportunity for PE firms to take stock – to see their industry through the lens of their peers and Dechert's own PE practice. Some 100 global firms were generous enough to give their time to this research. Taken in aggregate, their response provides a wide-ranging snapshot of the PE landscape.

The encouraging news is that a large percentage of these firms see good reasons to be positive about the future. While there is no shortage of obstacles to overcome, many firms are optimistic about both the short- and the longer-term outlook. There is appetite to raise funds, deploy capital and get back to the deal table – and widespread expectations that returns will be competitive.

We hope you find the data and opinions detailed in this year's report both refreshing and illuminating. This is an industry that has proved itself capable of outperforming in market conditions of every shade and color. We look forward to continuing to partner with our PE clients to help them capitalize on opportunities in 2025 and beyond.

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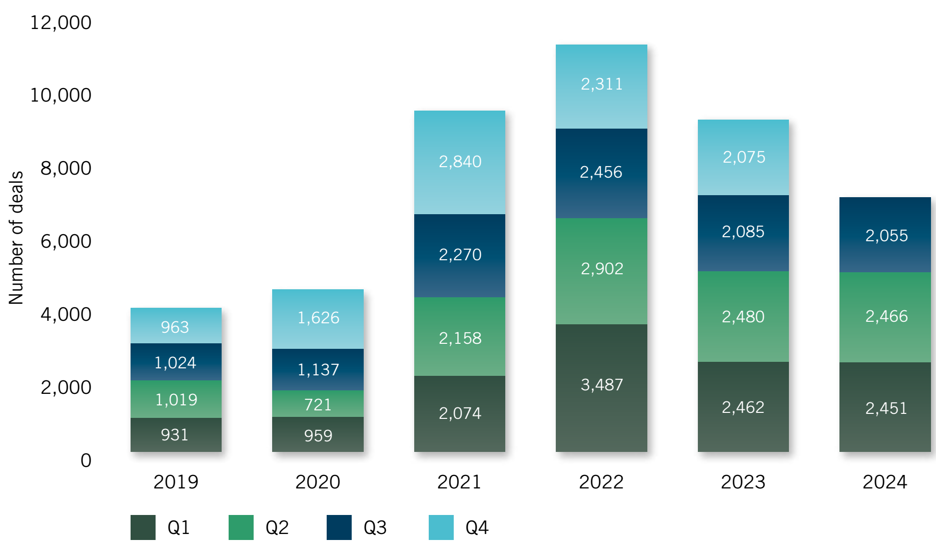
Introduction

After a slow start to the year, the global PE market has proved its resilience in 2024, and there is increasing optimism that 2025 has the potential to be even stronger. While PE firms' transactional activity over the past 12 months could not compete with the immediate post-pandemic period, it is likely to beat 2023's total, and it is also crucial to stress that dealmaking still looks extremely robust relative to the experience of the pre-pandemic years.

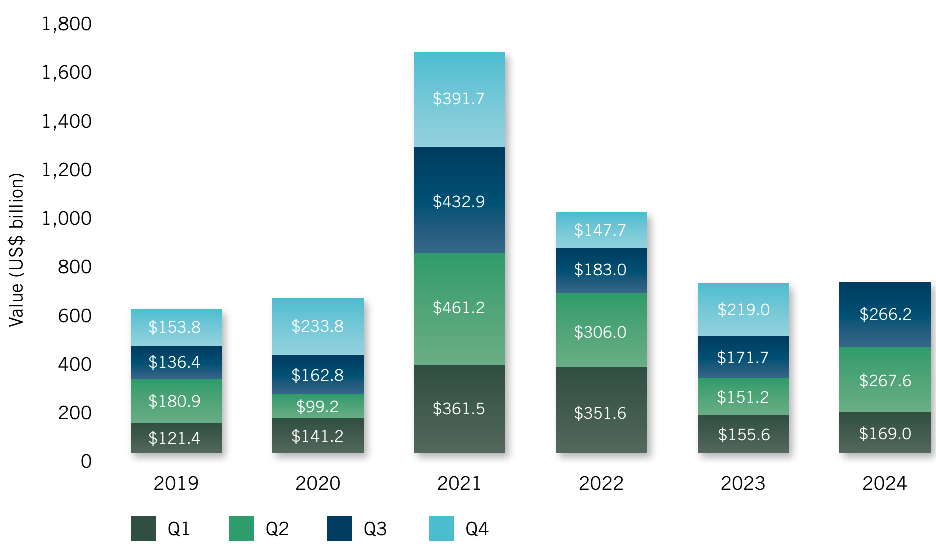
In volume terms, the first three quarters of 2024 saw 6,792 buyout transactions worldwide, representing just a 1% decrease on the same period in 2023, when PE firms were involved in 7,027 deals. However, looking back to 2019, the final full year of dealmaking before the pandemic struck, this year's figure looks notably stronger – in the first three quarters of that year, there were only 2,974 transactions.

In value terms, 2024 looks even healthier. The first three quarters of this year saw buyout deals worth US$703 billion worldwide. That is 47%

NUMBER OF GLOBAL BUYOUT DEALS, 2019–Q3 2024



VALUE OF GLOBAL BUYOUT DEALS, 2019–Q3 2024



up on the US$479 billion worth of transactions seen during the first nine months of 2023 – and far surpassing the totals for 2019 and 2020. The data reflects a surge in the number of megadeals, with 19 PE-backed transactions worth more than US$5 billion in the first nine months of this year.

Overall, the figures for 2024 point to genuine resilience in the PE sector, given the issues that dealmakers faced – particularly at a macro level, where the global geopolitical and economic backdrop were hardly supportive. With an expected further easing of interest rates and over US$3 billion of portfolio companies ready to be sold, there is potential for activity to continue growing. And with dry powder at record levels – global PE and venture capital funds held a total of US$2.62 trillion of uncommitted capital as of July 10, according to S&P Global Market Intelligence and Preqin – PE firms are ready.

There are no guarantees, of course. However, with the outcome of the U.S. election now known– and major elections across much of Europe and in India also concluded – the political picture has become relatively clearer in most developed markets, even if international tensions remain heightened. On the economy, meanwhile, the second half of 2024 has seen a decisive shift in much of the world, with central banks embracing looser monetary policies.

That has the potential to boost the PE sector throughout its entire cycle. Despite a challenging start to the year for liquidity events, exit volumes have also begun to improve with *Mergermarket* data revealing a 17% increase in activity for the first nine months of 2024 compared to the same period last year. Unblocking the exit logjam further will be the key to an even more active future.

A smoother road ahead?

In that context, there is a sense of genuine optimism for the next 12 months with a more settled political picture, at least in developed markets, and a brighter economic climate providing respite from a difficult dealmaking cycle.

In North America, Markus Bolsinger, co-head of Dechert's private equity practice, says: "It's certainly been mixed but there are now reasons to be optimistic about 2025, depending on who you ask and in which industries they work. This year started slowly but has been picking up pace consistently, although people were reluctant to take their feet off the brakes too swiftly ahead of the U.S. election in November."

In the Europe, Middle East and Africa (EMEA) region, Chris Field, co-head of Dechert's private equity practice, is also hopeful. "The system has been clogged," he says. "Exits haven't been happening as often because sellers were wanting prices that were too high to work for buyers when they put the numbers into their models; now that rates are reducing, the models start to look better, and the cycle begins to spin again."

In the same region, Sabina Comis, global co-managing partner of Dechert, adds: "The U.S. market has been quicker to recover thus far and we've been a little behind in Europe, but we can now follow that pick-up over the coming months."

Similarly, in the Asia-Pacific region, Dean Collins, managing partner of Dechert's Singapore office, says: "At the beginning of the year, people anticipated a real boost but we got off to a slow start; however, the second half of the year has been stronger, and the outlook is now improving – it appears to be a case of recovery delayed rather than derailed."

Speedbumps to navigate

Even with the optimism from the upturn in fortunes in the latter part of the year, downside risks are still present. The International Monetary Fund (IMF) is forecasting global economic growth of 3.3% for 2025, slightly above the 3.2% it notes was achieved during 2024. Equally, while interest rates are falling in many parts of the world, policymakers remain alive to the danger of inflation after the spikes of recent years – and will change course quickly if such pressures reemerge.

Meanwhile, in several locations, the geopolitical landscape remains volatile. The relationship between China and the West is still tense, while conflict flashpoints, including in Ukraine and the Middle East, are still a major concern.

However, despite the speedbumps, there are now signs of a smoother road ahead in many parts of the PE industry – and real reasons to believe that the industry can continue its upwards trajectory into 2025.

Key findings

U.S. ELECTIONS

31%

of North American respondents believe that the Republican victory in November's U.S. presidential election has the potential to boost portfolios, particularly for North American firms.

RETURNS

15.8%

The figure that PE firms, on average, estimate for their fund's net return for 2024.

FUNDRAISING

43%

of respondents highlight anxiety over geopolitical issues as the biggest obstacle to fundraising.

EXITS AND LIQUIDITY EVENTS

68%

of respondents believe market conditions for liquidity events will be unfavorable over the next 12 months, despite an upturn in exits in the latter part of 2024. This compares to 42% from last year's report. However, despite this somewhat downbeat assessment, exit activity has begun to increase in Q4.

CHALLENGES

34%

of respondents (up from 25% in last year's survey) feel that relatively weak economic growth is the biggest challenge facing the sector overall.

REGULATION AND ANTITRUST

21%

of respondents feel that more stringent regulation will have a major impact on the deal environment – this has slightly fallen from 30% last year but respondents note that the increasingly active stance taken by antitrust regulators will have a detrimental effect on activity.

CO-INVESTMENT

60%

of respondents globally now offer a co-investment program; in North America, 73% of firms offer co-investments.

PRIVATE CREDIT

63%

of respondents use private credit to support acquisition financing in their portfolios. Asset-backed securities (ABS) and other structured products are in use at 59% of global PE firms.

DEAL TRENDS

61%

of respondents describe club deals as very appealing in the current environment. This is up from 46% last year.

DEAL TRENDS

93%

of respondents are at least somewhat likely to consider take-private deals in the next 12 months, but since last year those who are "very likely" to has significantly dropped from 80% to 44% – perhaps due to the positive performance of the public markets.

BUY-AND-BUILD

60%

of respondents are focused on acquiring synergistic or complementary enterprises to drive their buy-and-build strategy forward, up from 47% last year.

ESG AND SUSTAINABILITY

100%

Every single respondent is considering investment activity related to sustainability and environmental, governance or social (ESG) factors, or are at least open to the idea.

GP-LED SECONDARIES

17%

of respondents expect to increase the use of GP-led secondaries. 71% of those looking to increase GP-led secondaries are driven by more lucrative opportunities for GPs. 82% of respondents expect secondaries activity levels to remain buoyant or increase in the next two years following 4x growth in the past five years.

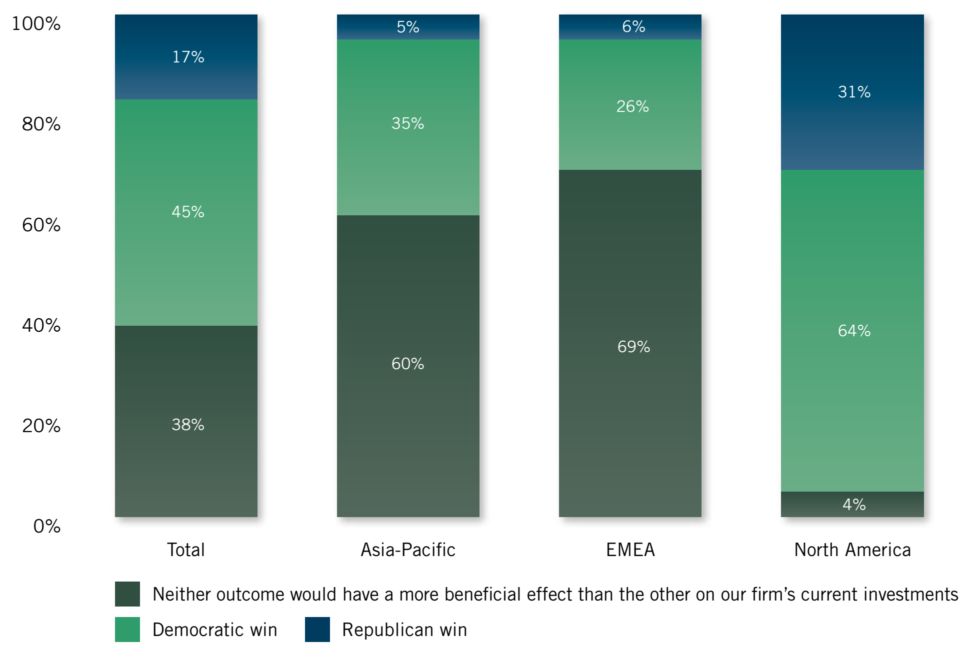
GP-STAKE DIVESTITURES

34%

of respondents are exploring GP-stake divestitures (down from 59% last year). 53% of those planning a GP stake divestiture will put the proceeds towards securing a larger commitment for a new fund.

U.S. election special

WHICH OF THE FOLLOWING OUTCOMES OF THE U.S. ELECTION DO YOU BELIEVE WOULD BE MOST BENEFICIAL TO YOUR FIRM'S CURRENT INVESTMENTS IN REGARDS TO RETURN ON INVESTMENT?



Donald Trump’s victory in November’s U.S. presidential election was remarkable, but our research suggests that its impact on the investments currently held by PE firms is likely to be less significant, particularly outside of the U.S. That said, there is some evidence that PE firms – particularly domestic investors – are concerned that President Trump’s second term in office will prove less supportive for their portfolios than a Kamala Harris victory would have delivered.

Prior to the election, 38% of PE firms taking part in our research felt that neither a Democratic nor a Republican election victory would have a more beneficial impact on their investments. Moreover, outside of North America, the figures were a great deal higher – at 69% and 60% in the EMEA and Asia-Pacific regions, respectively.

In contrast, domestic PE firms were naturally taking more of an interest in the outcome. Only 4% of North American respondents said the result would not make any difference to their portfolios. Almost two-thirds of North American PE firms in this research (64%) said they expected a Democratic victory to be more beneficial for their portfolio investments, against 31% who favored a Republican win in this regard.

One explanation for this split, suggests Bolsinger, is that PE firms were anxious about the uncertainties a Trump presidency might now entail. “It’s probably more predictable what would have happened under Harris, whereas that isn’t the case to the same extent with the incoming Republican government,” he says.

It is also the case that a Democratic administration would have been expected to be more interventionist, with further investment in areas such as clean energy, infrastructure and housebuilding. Harris had talked about building on the Inflation Reduction Act, described as the single largest investment in climate and energy in American history.

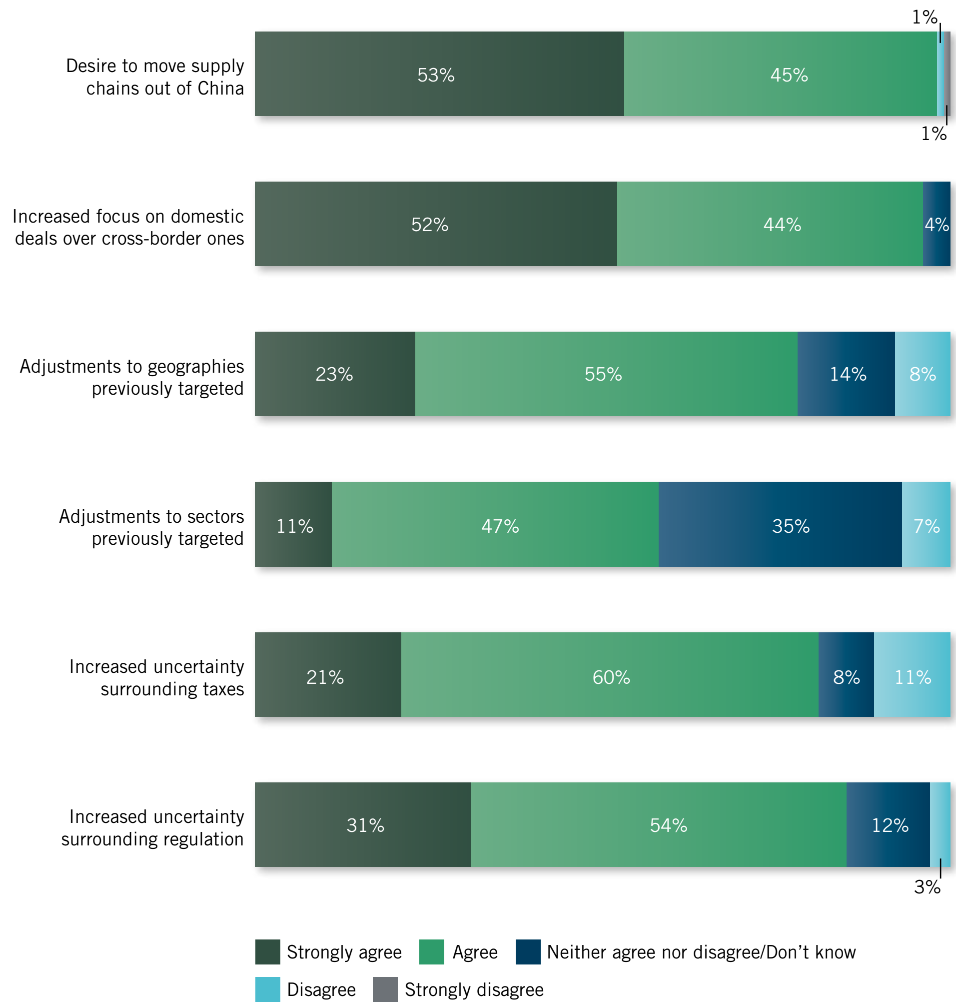
President Trump's efforts to support the U.S. economy will more likely be channeled through tax cuts, both for corporates and individuals. While this does have the potential to drive growth in several areas, there is also concern that the inflationary impacts of tax cuts could prompt an intervention from the U.S. Federal Reserve, with interest rates once again moving towards an upwards trajectory. That would disappoint many investors, given the Fed's move to reduce rates by 50 basis points in September (its first reduction in four years) and 25 points in November; that lowered its target rate to 4.5%-4.75%.

Overall, respondents do not appear to expect positive news on tax during President Trump's second term, with 81% concerned about increased uncertainty on this issue. This likely reflects the president's campaign promises to introduce high tariffs on imports of many foreign goods, which would, according to many economists, raise prices for middle-class consumers. Such tariffs therefore amount to the equivalent of an additional sales tax, potentially reducing consumption.

A more conventional approach

It's also striking that 85% of PE firms are concerned about increased regulatory uncertainty under President Trump, who has previously stressed the importance of reducing red tape on large parts of the business sector.

IF THE REPUBLICANS WERE TO WIN THE 2024 U.S. ELECTION, TO WHAT EXTENT DO YOU AGREE OR DISAGREE THAT YOUR INVESTMENT PLANS WOULD BE AFFECTED IN THE FOLLOWING WAYS? (SELECT ONE FOR EACH ROW)



That likely reflects the President's more protectionist rhetoric, particularly toward trade partners such as China. However, domestic businesses in sectors such as oil and gas may feel more positive about what lies ahead, with the President on record as supporting the conventional energy sector. During the campaign, it emerged that oil and gas interests had donated roughly US$11 to Trump for every US$1 donated to the Democratic nominee.

In other areas, meanwhile, many PE firms appear to believe there was little to choose between the two sides, with a more protectionist and nationalistic agenda regarded as likely whatever the outcome.

For example, 98% of firms now anticipate further pressure to move supply chains out of China under President Trump, but 92% said they believed a Harris presidency would have had a similar impact.

Similarly, 96% and 88% of PE firms respectively predicted, prior to the election, that a Republican or Democratic victory would drive an increased focus on domestic deals as opposed to a pick-up in cross-border M&A.

The survey findings underline one of the ironies of the election – that despite the polarization of a vituperative campaign, neither side was proposing radical trade or economic policies that represented a major departure from the Biden administration.

Indeed, PE firms appeared to recognize that irrespective of the outcome of the vote, the post-election period would be characterized by a persistence of foreign tariffs, infrastructure projects and deficit spending. That has positive implications for domestic companies as production is brought back to the U.S.

For most PE firms, portfolio strategy is therefore likely to be tweaked in the months and years ahead rather than overhauled. More than three quarters of the firms taking part in this research (78%) are likely to make adjustments to geographies previously targeted – but less than a third of these respondents feel strongly in this regard.

> PE is a mature industry that has shown over many decades that it can deal with whichever way the political wind is blowing – investors will focus on what they can control.

Markus Bolsinger
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Fund trends

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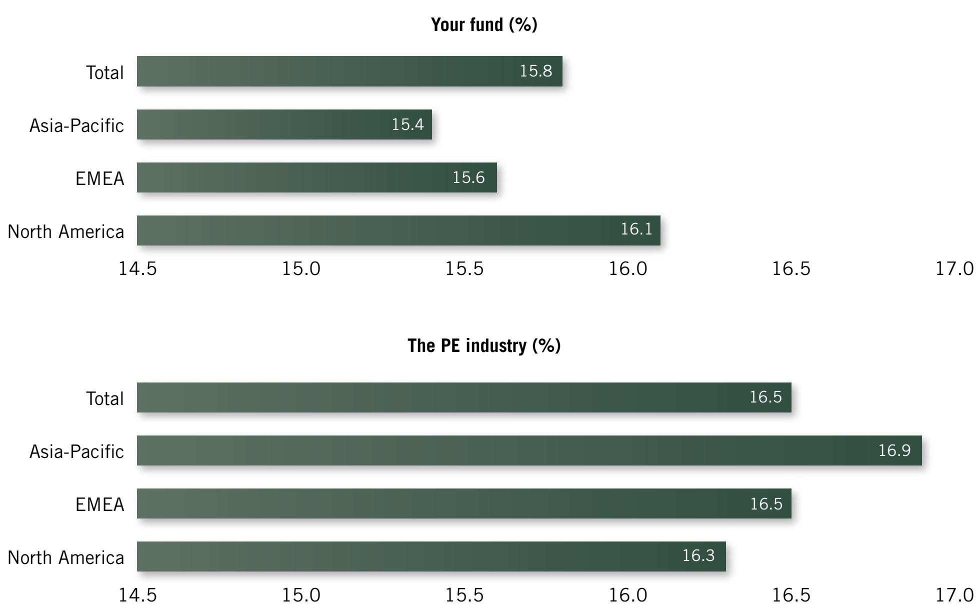
In a world where economic and geopolitical challenges remain pressing, PE firms are cautious about the outlook for the year ahead. They note continuing inflationary pressures in many parts of the world – and the implications of that for tighter monetary policy – as well as escalating trade tensions and ongoing political volatility. The decision by several central banks, including the Fed, the ECB, the Bank of Canada and the Bank of England to cut interest rates in the late summer and early fall provided comfort, but rates remain higher in comparison to much of the past 15 years.

The good news is that investment returns appear to be holding up. On average, the PE firms taking part in this research estimate their fund's net return for 2024 at 15.8%. North American funds are more optimistic, with respondents in the region citing an average return of 16.1%. But regional variations are relatively limited – the equivalent figures for the EMEA and Asia-Pacific regions were 15.6% and 15.4%, respectively.

One nuance here is that while PE firms with funds based in North America think their funds' performance is broadly in line with the net returns achieved by the PE industry overall, their counterparts in Asia-Pacific and EMEA are more likely to think they have lagged. Most strikingly, the average Asia-Pacific respondent estimates their fund's net return is 1.5 percentage points lower than the average fund globally. While there is no definitive rationale for the discrepancy, some respondents report frustrations with the difficult exit market in Asia-Pacific generally and exit prices they have been able to achieve.

"It is tough to find the right buyers for our assets," a partner in one Hong Kong PE firm explains. "Even though we've worked hard to make these assets attractive, exit conditions have been bleak." More broadly, investors in the region note that valuations have been especially volatile, adding to exit challenges;

WHAT DO YOU ESTIMATE THE NET RETURN FOR 2024 TO BE FOR...?



in addition, a number of prominent IPOs have also disappointed.

Indeed, a certain degree of realism is important here, argues Comis. "There is a danger in being too optimistic about returns, given the valuations that investors are still having to settle for on exit," she warns. "It's easy to forget that during the sector's big boom years, returns probably got ahead of themselves; maybe we're back to where we should be now."

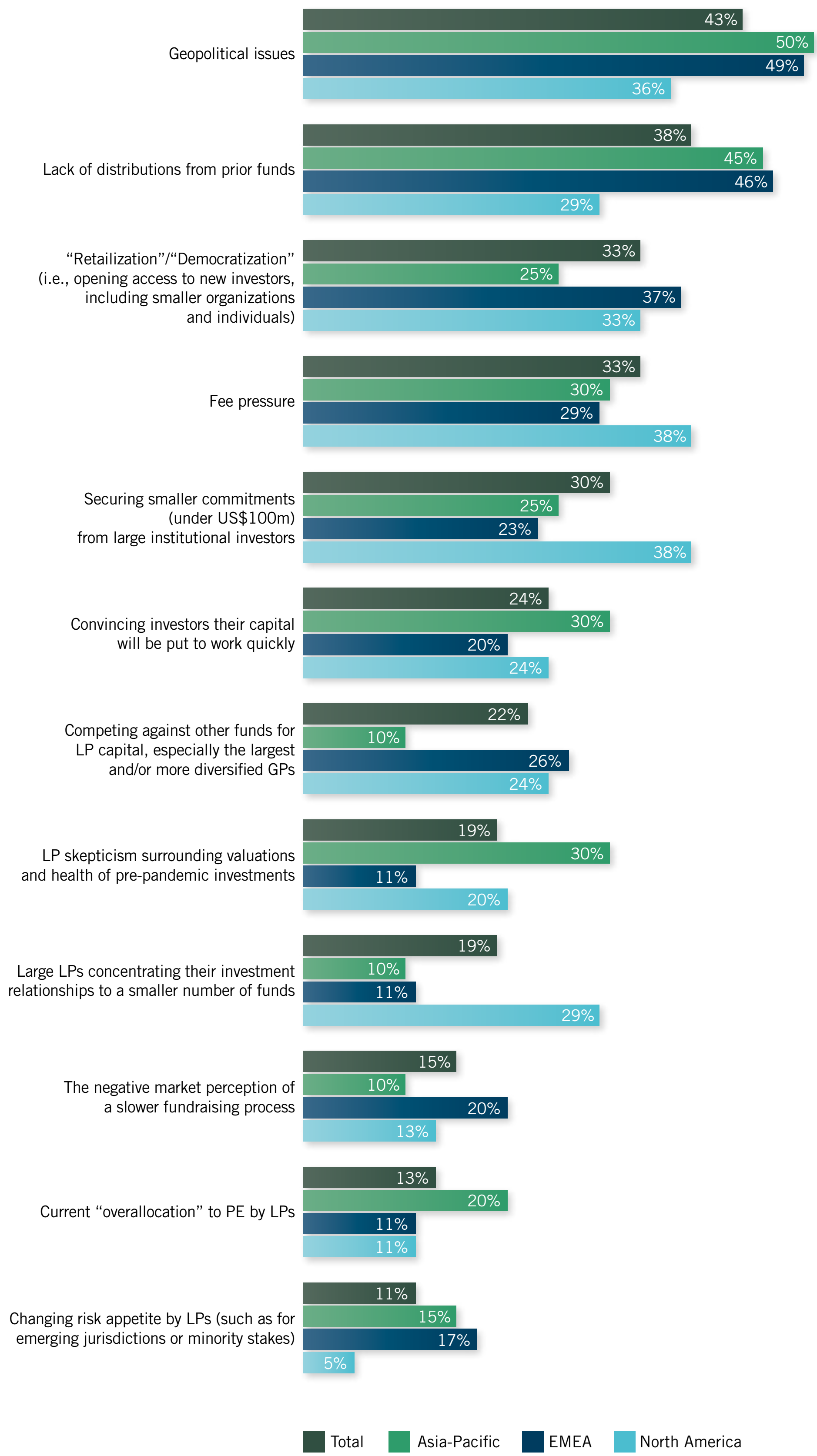
Geopolitics hampers fundraising

Similarly, when it comes to the prospect of raising new funds, many PE firms still envision significant obstacles. At the top of the list of challenges, sponsors in all three regions point to geopolitical issues such as the plethora of elections taking place this year, most notably in the U.S. This is a significant increase compared with last year's report, where only 6% saw geopolitical risk as their biggest challenge to fundraising.

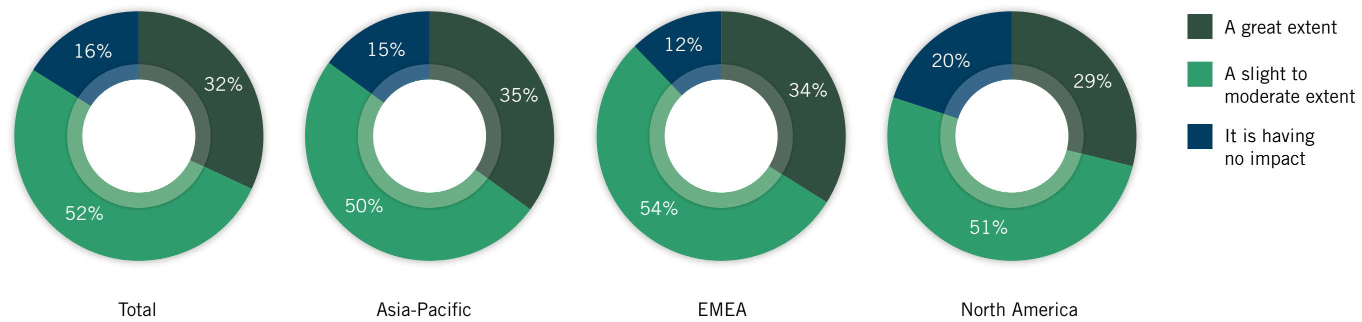
Clearly, the uncertainty and volatility caused by conflicts in the Middle East and Ukraine, and by the strained relationship between China and the West, are continuing to cause real concern.

"Geopolitical issues are a particular factor in Asia-Pacific and EMEA," notes Sam Kay, Dechert partner, financial services, London. "Clearly, the tensions between the U.S. and China and the retreat from globalization are making it harder to fundraise in the Asia-Pacific region from certain types of investors. It also appears that the subdued

WHAT IS THE BIGGEST GLOBAL FUNDRAISING CHALLENGE YOUR FIRM HAS FACED? (SELECT UP TO THREE)



TO WHAT EXTENT DO YOU THINK THE RETAILIZATION/DEMOCRATIZATION OF PRIVATE EQUITY WILL HAVE AN IMPACT ON FEE STRUCTURING? (SELECT ONE)



economic outlook in Europe and political instability with the rise of populist and far-right policies are creating fundraising challenges in EMEA."

Indeed, during the first three quarters of 2024, PE firms globally raised US$589.9 billion in new capital, according to data from Private Equity International. This is down from US$672.5 in the same period last year. However, it is worth noting that this is still well above pre-pandemic levels.

Blockages in the pipeline

Other challenges in fundraising are more specific to the PE sector. In the EMEA and Asia-Pacific regions, for example, many investors appear capital constrained, as the difficult market environment of the past couple of years has resulted in funds not distributing cash as quickly as investors anticipated, reducing liquidity available to deploy to new funds; in North America, where the sector's recovery appears more advanced, this is somewhat less of an issue.

Fee pressure is also a concern – and here, North American PE firms highlight they are likely to see this as a bigger challenge than their regional peers, with 38% citing it as a major obstacle. The debate around fund access is also causing some difficulties. A third of respondents (33%) overall cite "democratization" as a barrier to fundraising, perhaps because broader raises are more challenging and time-consuming, with firms having to restructure back-office capabilities to accommodate this change. This also has the potential for fee compression.

"The retail market often sees greater price sensitivity and demand for lower-cost investment options," says Kay. "This pressure can force private fund managers to offer more competitive fees to attract investors more used to 'retail' products."

However, democratization can also be a mitigation strategy – simply because a broader investment audience for a given vehicle increases its chances of hitting its fundraising targets.

While PE firms recognize this, they are concerned about the implications around fees. Overall, 84% of respondents warn democratization is having a negative impact on fee structuring, including 32% who describe this impact as significant. "In order to raise a retail fund, often private fund managers need to work with an intermediary, such as an insurer or a private bank," says Comis. "This means that the fund managers need to share the fee with a number of additional players."

Meanwhile, in North America, PE firms are particularly worried about securing smaller commitments from large institutional investors (38%). This is almost double the figure from 2023. Kay says: "This is likely down to a lack of prior distributions to institutional investors, which means it's more likely those investors will have less available capital so will only make smaller commitments to new funds."

Innovative thinking

To overcome such challenges, PE firms are having to be flexible and imaginative, employing a range of tactics to navigate through fundraising obstacles. Above all, more than half (59%) are now expanding into different investment strategies, broadening their appeal to existing investors or targeting new limited partners (LPs).

"I'd expect to see more minority deals over the next year," says one partner of a Hong Kong PE firm now looking at diversification.

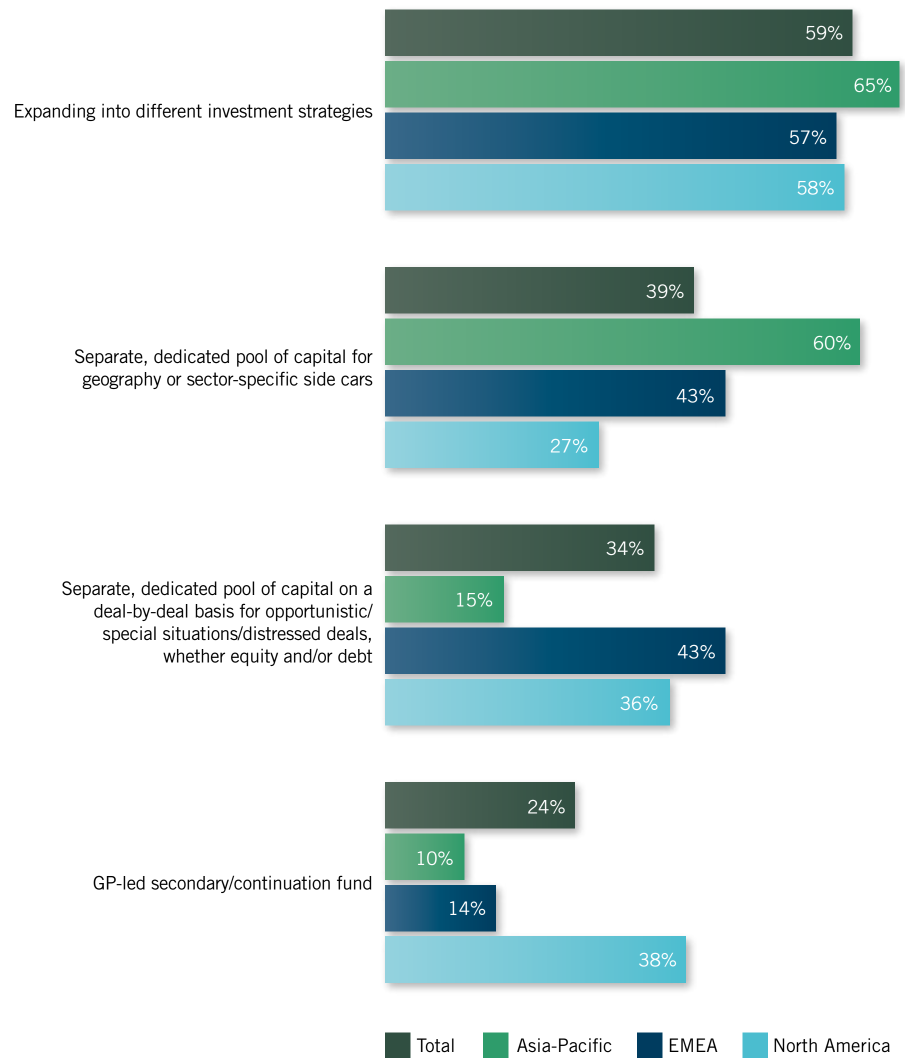
In North America, a U.S. partner adds: "The number of earn-out structures will increase in the coming months – these provide effective solutions to deal with the larger valuation expectations."

There are regional variations in terms of responses. In Asia-Pacific, for example, PE firms are particularly likely to see the merits of more targeted investment propositions, with 60% launching separate pools of capital specifically dedicated to particular geographies or sectors. "This may reflect a desire from investors for a greater degree of customization to gain further exposure to high-growth economies in the Asia-Pacific region," says Maria Tan Pedersen, co-head of Dechert's emerging markets practice.

In EMEA, where the economic picture has varied considerably from one country to another over recent months, 43% of firms are taking a similar approach on a deal-by-deal basis.

In North America, meanwhile, 38% of PE firms point to the value of GP-led secondary or continuation funds. If traditional exits are challenging, making it difficult for PE firms to work through previous funds and raise new ones, it can work well for GPs to facilitate the sale of

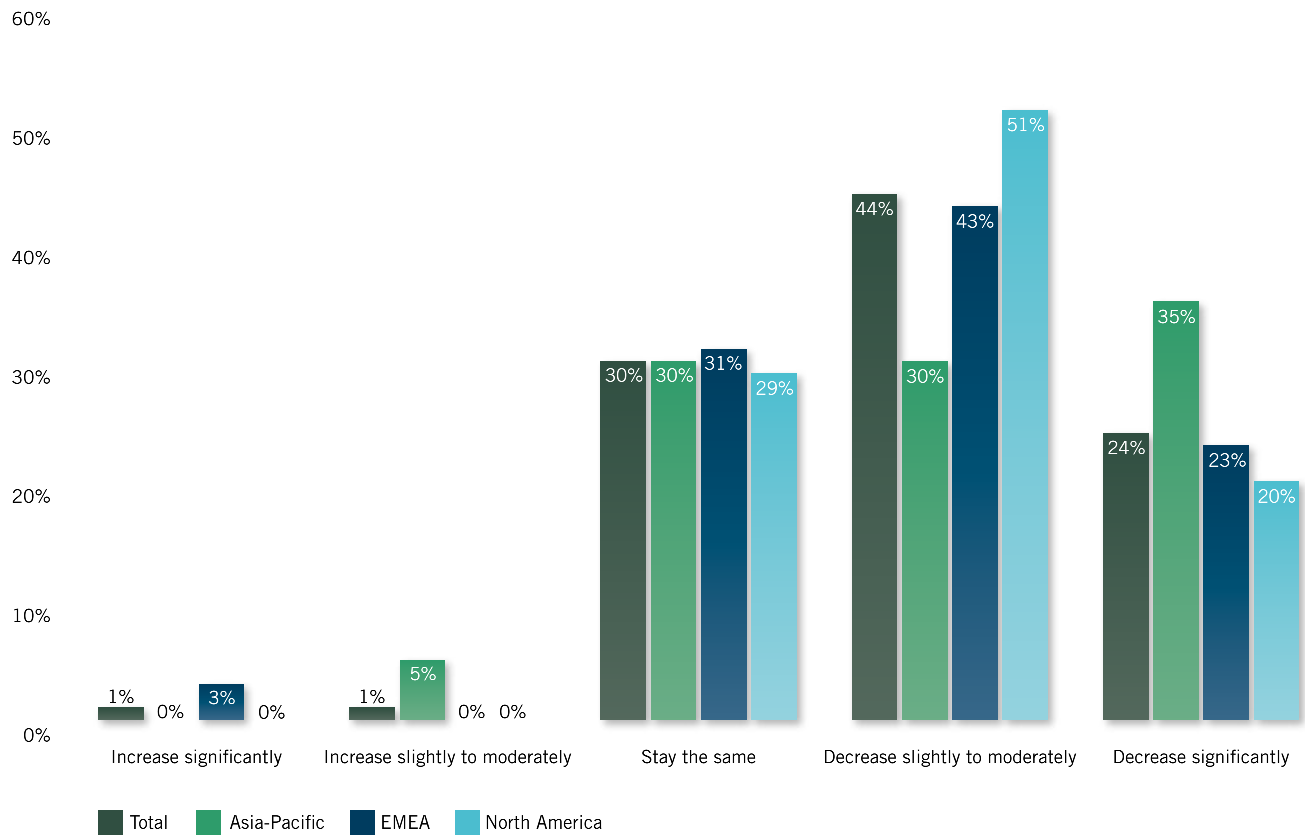
WHAT STRATEGIES IS YOUR FIRM EMPLOYING TO NAVIGATE THE CURRENT FUNDRAISING CHALLENGES? (SELECT ALL THAT APPLY)



> "The democratization of PE will continue – and the fund industry is less likely to follow the historical divide between open-ended and close-ended funds."

Sabina Comis
Dechert LLP

DO YOU EXPECT FUND FINANCE TO INCREASE OR DECREASE IN 2025?



portfolios from one set of LPs to their successors.

"The growing trend of setting up continuation funds also offers an alternative to allow firms to continue holding and developing investments while potentially returning some capital to initial investors," says Comis.

Fund finance falls

A final trend to note is that, as concern about exits and fundraising begins to ease, PE firms expect the use of fund finance to correspondingly reduce. More than two-thirds of respondents (68%) anticipate a fall in fund finance during 2025, including 24% who expect significant decreases. North American respondents are particularly likely to anticipate reduced levels of fund finance over the year ahead.

"In a higher interest rate environment, subscription line and NAV facilities are more expensive and so less attractive," says Kay. "But even with the expectation of interest rates stabilizing or falling, GPs are still contending with market volatility, leading to reduced confidence in leveraging strategies, tighter credit conditions impacting the number of lenders offering attractive terms, and increased regulatory scrutiny."

That said, while acknowledging the data, Comis points out that 30% of respondents expect fund finance to remain at current levels, with broadly similar numbers of PE firms in all regions taking this view. "There is not always a consensus between investors and fund managers as to whether NAV facilities are ultimately favorable to the investors, but they are here to stay for now, particularly in Europe," she says.

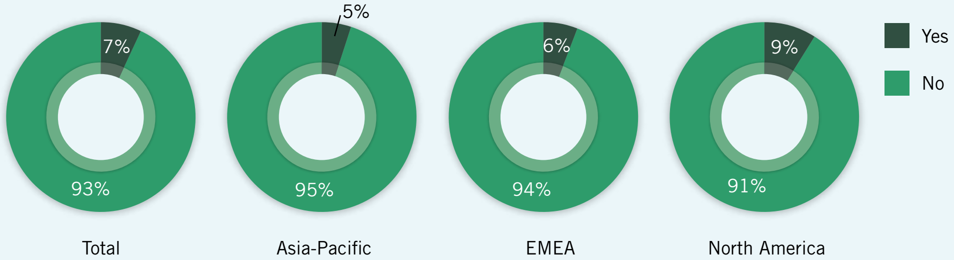
Management companies: To list or not to list?

PE management company listings remain relatively rare, but CVC's IPO on Amsterdam's Euronext in April 2024 has once again prompted interest in this strategy. In our research, 9% of North American PE firms say they are considering listing their management company, falling to 6% and 5% in the EMEA and Asia-Pacific regions, respectively.

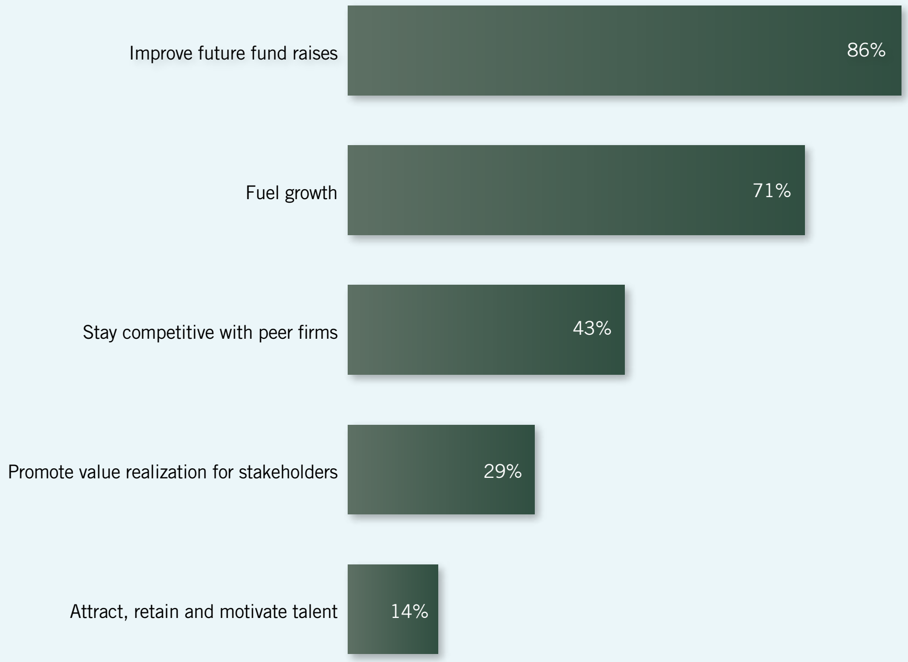
Such deals have both upsides and downsides. A listing can boost the profile of a PE firm and provide valuable new balance sheet capital – at a premium when fundraising is more challenging. On the downside, such deals upend the traditional partnership model, with shareholders entitled to at least a share of fee income.

PE firms considering an IPO are focused on the upsides: 86% point to the potential to improve future fund raises, while 71% think a management listing could fuel their growth. "It's also significant that 43% of PE firms considering this option see it as enabling them to remain competitive with their peers," says Pedersen. "They're looking at the rivals that have gone down this route and they don't want to lose out," she says. "There are only so many firms large enough to pursue this option, but some of the megafunds see its value."

ARE YOU CONSIDERING LISTING YOUR COMPANY?



IF YOU ARE CONSIDERING LISTING YOUR MANAGEMENT COMPANY, IS IT TO...? (SELECT ALL THAT APPLY)*



*Question only given to those who stated they are considering listing their management company

Deal environment: Challenges and impacts

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Brenda Sharton
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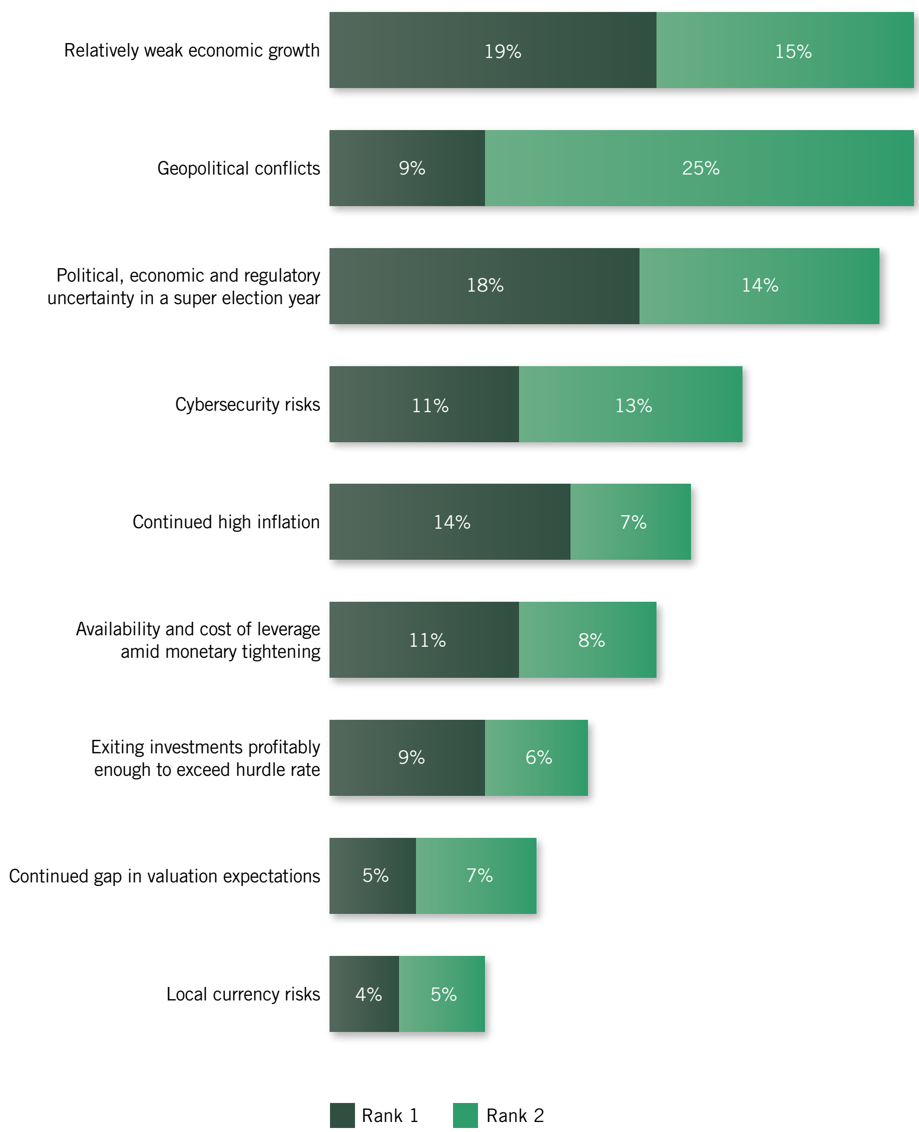
Although interest rates are slowly reducing and the run of global elections is now at an end, economic issues are still taking center stage for the PE sector as it considers the challenges it currently faces.

Overall, more than a third of PE firms (34%) now regard relatively weak economic growth as one of the two biggest challenges currently facing the sector. With large numbers of respondents also citing the economic uncertainties of an election year, persistently high inflation and the potential for tighter monetary policies, it is evident that the wider economic backdrop and current geopolitical climate is giving PE firms pause for thought.

And pessimistic pronouncements from forecasters and policymakers only add to the uncertainty. The World Bank, for example, has warned that during 2024 and 2025, global economic growth will underperform its 2010s average in nearly 60% of economies worldwide, accounting for more than 80% of the world's population. It warns that "downside risks predominate, including

WHAT DO YOU SEE AS THE BIGGEST CHALLENGES CURRENTLY FACING THE PRIVATE EQUITY INDUSTRY? (SELECT TOP TWO AND RANK 1-2, WHERE 1 IS THE BIGGEST CHALLENGE)



geopolitical tensions, trade fragmentation, higher-for-longer interest rates and climate-related disasters."

However, there are also reasons for optimism. Inflation is easing in many countries, to the extent that central banks in both North America and Europe have felt able to move toward interest rate deductions. In addition to the Fed, the European Central Bank cut its key deposit rate in both June and September, reducing this to 3.5%. The Bank of England (BoE) returned to rate-cutting in August, with a narrow majority of the Monetary Policy Committee backing a 0.25 percentage point reduction to 5%. The BoE reduced rates by a further 0.25 percentage points in early November.

Meanwhile, political uncertainty is subsiding after a year in which over half of the world's population had an opportunity to vote in elections.

Moreover, PE firms have taken steps to counteract certain macro challenges, points out Bolsinger, both in their own investment activity and through their work with portfolio businesses. Of the former, Bolsinger says: "People are looking much more closely at geopolitical risk as they think about how and where to invest – in the Asia-Pacific region that might mean increasing allocations to Japan, for example, which is seen as more Western-friendly." Indeed, Japan's PE market continued to impress during the first nine months of the year after a robust 2023; leading deals included the US$388 million buyout of BigMotor Co by Itochu Corp and J-Will Partners.

> There are so many variables at play, but there is good reason to think 2024 will prove to have been stronger than 2023, and that 2025 may be even stronger.
>
> **Chris Field**
> Dechert LLP

Dealing with portfolio challenges

On PE firms' portfolio investments, Bolsinger adds: "They're taking a strategic view – by curtailing their relationships with China, perhaps, or by 'friend-shoring' their supply chains, and that process is going to continue." For example, Japanese electronics giant Toshiba, now owned by Japan Industrial Partners, has moved production from China to other countries, including Thailand and India.

Equally, however, Bolsinger urges PE firms not to become so preoccupied by big-picture macro issues that they miss emerging risks. "For example, there should be concern about the commercial real estate market," he warns. "Real estate debt is often held by smaller, more local banks and some of them have a large number of their eggs in that single basket."

Dean Collins is also keen to see more evidence of PE firms coming to grips with market concerns. In our research, only 15% of respondents cite one of the sector's biggest challenges as the difficulty of exiting investments profitably enough to exceed target hurdle rates; and only 12% point to the gap between the expectations of buyers and sellers on valuations.

"I think people believed valuation expectations would come down more quickly because sellers simply wouldn't be able to wait that much longer to exit, but buyers appear to have been unexpectedly cautious," he says. "On the positive side, the pressure to exit and the pressure to invest has begun to grow and the prospect of falling interest rates is also helping."

There is also work to be done on the internal challenges that the industry faces. Almost a quarter of firms (24%) said that cybersecurity risks now represent one of the two biggest challenges faced by the industry. Yet reports show not all firms are confronting this issue. One recent survey found fewer than a quarter of PE firms have an operational and compliant cybersecurity program.

Deal activity can leave PE firms particularly vulnerable to cyber-attacks, with Accenture reporting that 68% of firms see an uptick in incidents during the month of a deal closure.

"The public announcement of a deal often brings out the threat actors, who are opportunistic, and hope to capitalize on vulnerabilities that might arise as the systems of the two companies are integrated, especially when there is sophistication disparity in the cybersecurity programs. Threat actors also will phish unwitting employees, who may not yet know the acquirors' high-level executives," says Brenda Sharton, litigation partner and chair of Dechert's top-ranked, global cybersecurity, privacy & AI practice.

Sharton notes: "This often will come in the form of a spoofed communication or voice reach out purportedly from the new CEO or other high-level executive. And with the assistance and proliferation of AI, these can often seem very credible. As you integrate, it is important not to connect the systems of the target company until you are certain that its cybersecurity program is at an appropriate risk level, and that you train employees to be on high alert for phishing emails purportedly sent on behalf of the new leaders."

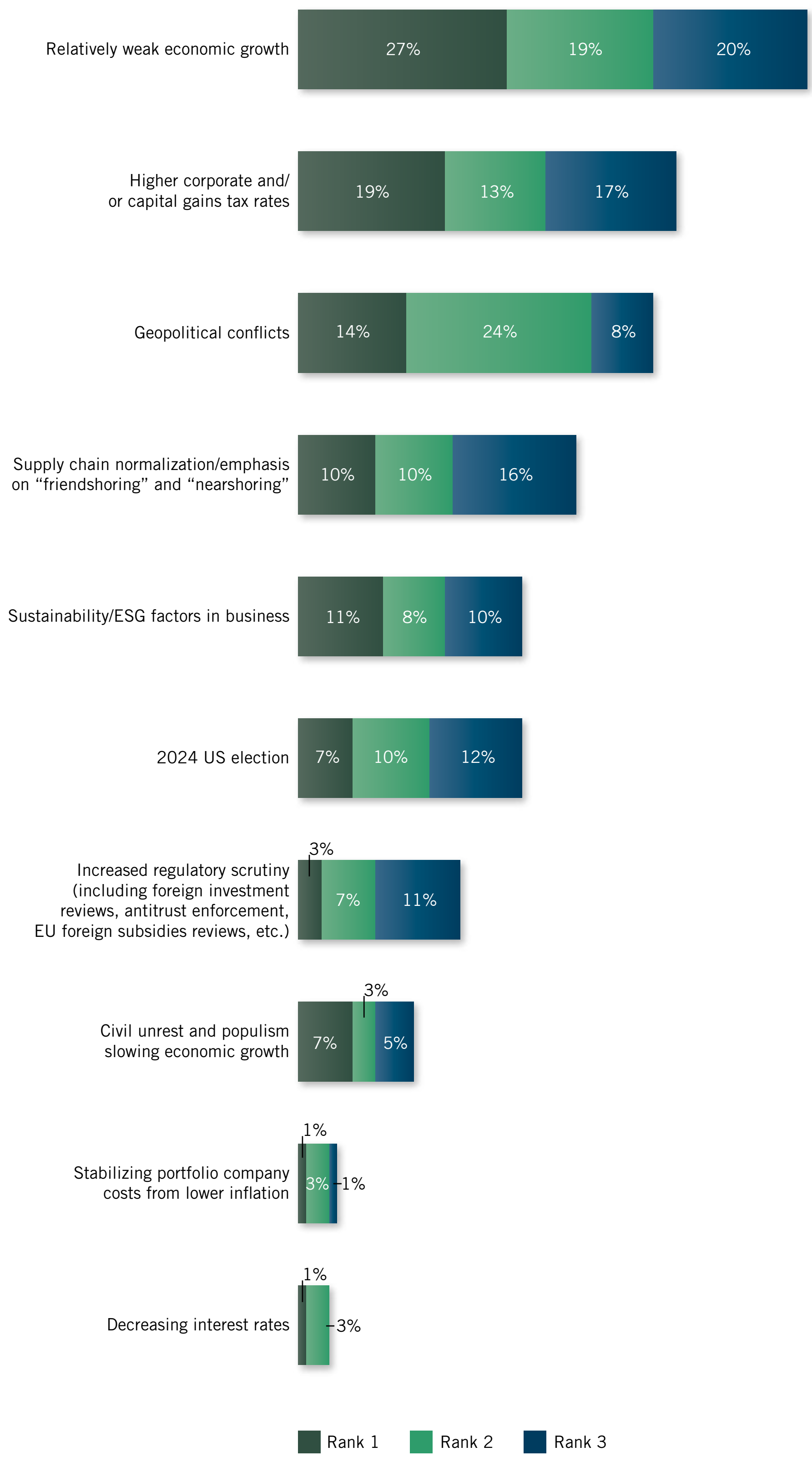
Worldwide, cybercrime costs are set to reach US$10.5 trillion by 2025.

What lies ahead?

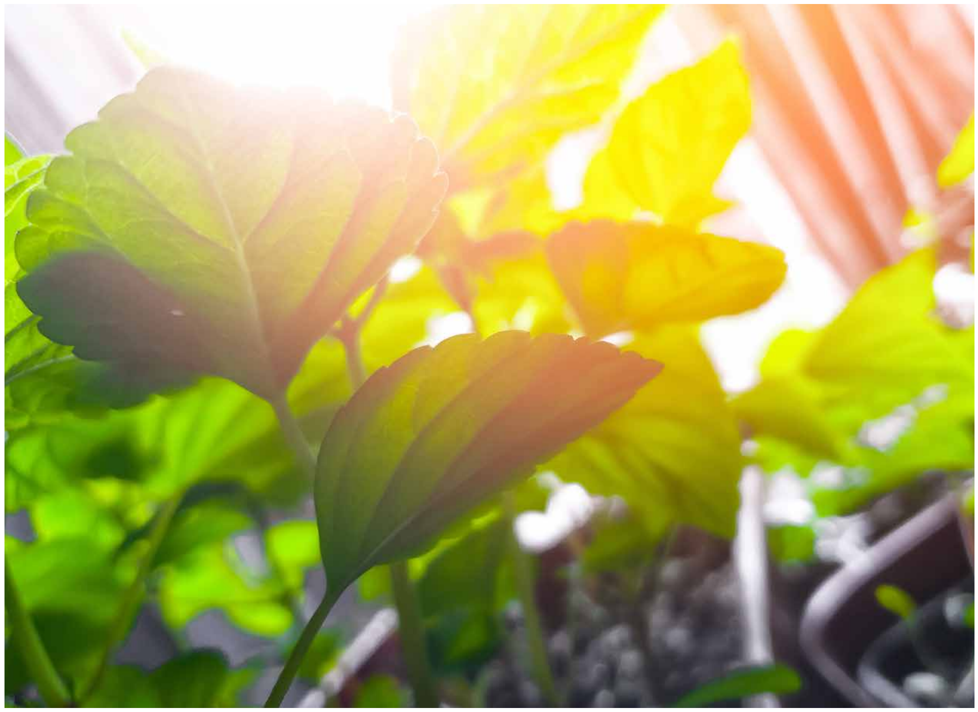
In the short term at least, some of these challenges are almost certainly going to persist. Asked which drivers they expect to have the biggest impact on the deal environment over the next 12 to 18 months, two-thirds of firms (66%) – up from 31% last year – single out the likelihood of relatively weak economic growth as one of the three most significant, including 27% that expect this issue to have the greatest effect.

Similarly, geopolitical conflict is expected to be an ongoing drag on the deal environment, with little end in sight to an alarming number of seemingly intractable global conflicts. Almost half of PE firms (46%) cite this as one

IN YOUR ESTIMATION, WHICH CURRENT OR UPCOMING DEVELOPMENTS WILL HAVE THE BIGGEST EFFECT ON THE DEAL ENVIRONMENT OVER THE COMING 12-18 MONTHS? (SELECT TOP THREE AND RANK 1-2-3, WHERE 1 IS THE GREATEST EFFECT)



of the three biggest impacts on the market over the near term, including 14% who see it as the most important driver of all. This is a 25 percentage-point increase from last year.



Elsewhere, higher tax rates – potentially both for corporates and for investors (through capital gains taxes) – are also weighing heavily on many PE firms' minds. Almost half (49%) believe these will have a major effect on the deal environment in the next 12 to 18 months.

On corporate taxes, the OECD reports that after a long period in which average rates have declined on a global level, this trend has now flattened out, with some countries now moving in the opposite direction.

On capital gains tax (CGT), several countries are reported to be looking at higher levies – including the UK, where the new Labour government has raised CGT in the October Budget. "While it is somewhat overblown in some quarters, there is still a valid concern about which way policymakers such as UK Chancellor Rachel Reeves are deciding to jump," says Field.

Green shoots begin to spring

Taking these issues in aggregate, the concern must be that they continue to curtail deal activity – keeping exits lower than expected and therefore blocking the natural cycle of realizations and fundraisings.

"The big issue has been the meaningful absence of exits, though the tide is starting to turn," says Field. "Although we've seen a variety of alternative liquidity solutions emerge to try to plug the gap, they are not a complete solution and have often just kicked the can down the road."

Indeed, after a slow start to 2024 and a lackluster 2023, exits have begun to take an upward trajectory. Volumes for the first nine months of 2024 are up 17% on the same period last year, although noticeably down in 2021 and 2022.

Field believes that looser monetary policy is beginning to resolve the blockage. "Exits were not happening because the buy side has been asked to pay prices at a level where its model doesn't work," he says. "So, with the reduction of rates, things start looking better in the model and the system begins to spin – there is a long way to go, but we are beginning to see green shoots."

Confidence, naturally, will take time to return – it is noticeable that only a fraction of respondents cited decreasing interest rates as among the developments that would have the biggest, near-term effect on the deal environment. Still, as broader macro pressures subside, a recovery is likely to take hold, particularly as firms have record levels of dry powder and are under pressure from LPs to deploy it. "2024 began reasonably slowly, but the pace has picked up quickly – the brakes may come off now that the U.S. election has been decided," says Bolsinger.

> "PE firms are fully aware of the challenges, and they're really drilling into the fundamentals to respond in the right way."
>
> 
>
> **Maria Tan Pedersen**
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Regulatory scrutiny: Antitrust to the fore

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Rising regulatory scrutiny continues to be a concern for many PE firms. More than a fifth (21%) regard developments in this space as likely to be one of the three biggest impacts on the deal environment over the next 12 to 18 months. Indeed, while regulation may not be the top issue for many respondents to this survey, it is a consideration that consistently ranks highly in their list of concerns.

One crucial aspect of this is the increasing focus on competition issues in many areas of the world. In the U.S., for example, the Federal Trade Commission (FTC) and the Department of Justice (DOJ) Antitrust Division have broadened the scope of investigations to include novel antitrust theories, such as the harm a merger may cause on labor markets. In addition, U.S. antitrust agencies have developed new requirements for antitrust filings that could substantially add to the burden and timing of obtaining antitrust clearances. The Dechert Antitrust Merger Investigation Timing Tracker (DAMITT) found the average duration of significant investigations in the U.S. ticked up to 11.0 months during the first half of 2024, from 10.6 months for 2023.

"Early preparation and planning for antitrust scrutiny has to start with the transaction agreement," suggests Rani Habash, Dechert partner, Antitrust (Washington D.C.). "Antitrust risk-shifting provisions can be tailored to enable buyers and sellers to limit risk according to their appetite."

In Europe, several national competition watchdogs have expanded their remit within recent years. "National enforcers in the EU are as active as ever," says Clemens York, Dechert partner, Antitrust (Brussels, Munich). "The complexities of European merger approval (including the possibility of referrals to and from the European Commission) need to be adequately reflected in the deal documents."

In the Asia-Pacific region, a new competition regime has come into force in Australia, with India, China, Indonesia and Taiwan all making significant changes to their antitrust regulations.

The result, highlights Bolsinger, is that PE firms are now having to think about antitrust issues in a much broader range of potential transactions – and often at the very outset of a deal. "People are spending more time either preparing for or looking at antitrust much earlier than they have in the past," he says. "There are deals where the first call that people make is about figuring out the antitrust sensitivities."

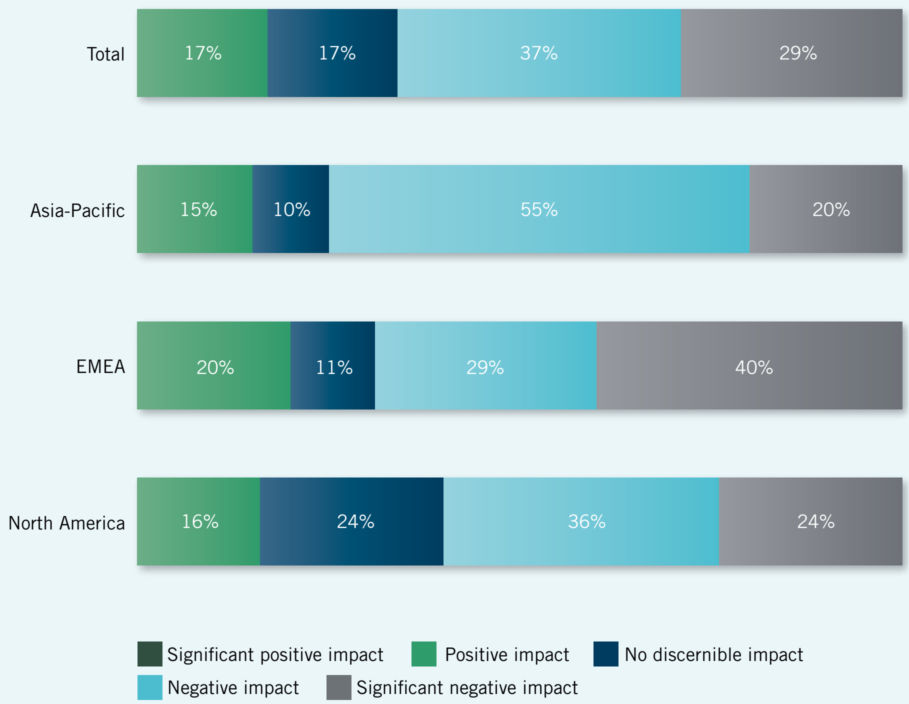
Our research underlines the point. Globally, two-thirds of PE firms (66%) expect increased scrutiny from antitrust authorities to have a negative impact on their dealmaking plans over the next 12 months; that includes 29% who anticipate a significant negative impact.

Concern is particularly marked from respondents in the Asia-Pacific region – with 75% worried about more scrutiny to come. Meanwhile, over two-thirds (69%) of EMEA respondents feel that greater scrutiny will have a negative impact on dealmaking plans.

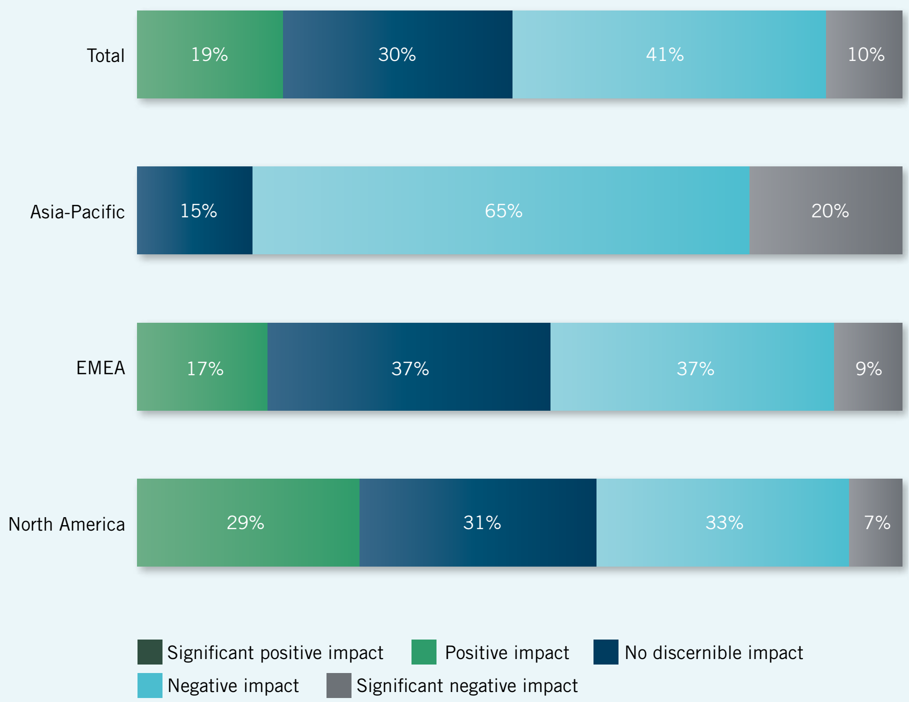
In North America, 60% of PE firms fear their deals could be negatively affected by antitrust scrutiny. That the figure is lower than in other regions may reflect uncertainty over the outcome of the presidential election, since this research was conducted before the result was known. But regulation is certainly ramping up in the region. Canada has recently completed a wave of amendments to its competition law that fundamentally changes its landscape. In the U.S., high-profile antitrust inquiries into leading technology companies have been announced or rumored; and in the healthcare sector, antitrust authorities have expressed skepticism of PE ownership of healthcare entities and even launched a lawsuit against at least one PE firm for its alleged involvement in developing a provider roll-up strategy.

This is not to suggest that antitrust regulation is always a headwind for the PE sector. Indeed, 17% of respondents expect increased competition scrutiny to have a positive impact on their firm's dealmaking plans. It may be that these firms expect less competition from larger buyers for certain assets; moreover, where competition inquiries lead to divestments or break-ups, PE buyers are often in a strong position to step in to make acquisitions – potentially at attractive prices.

HOW DO YOU EXPECT GREATER SCRUTINY FROM ANTITRUST AUTHORITIES TO IMPACT YOUR FIRM'S DEALMAKING PLANS OVER THE NEXT 12 MONTHS?



WHAT IMPACT DOES INCREASED FOREIGN INVESTMENT AND NATIONAL SECURITY RELATED SCRUTINY FROM REGULATORY AUTHORITIES HAVE ON YOUR FIRM'S WILLINGNESS/ABILITY TO ENGAGE IN DEALS OVER THE NEXT 12 MONTHS? (SELECT ONE)



The role of national security

A related issue to the antitrust question is the growing influence of regulatory bodies that have a mandate to consider national security or foreign direct investment (FDI) issues in the context of dealmaking, particularly for cross-border transactions.

"As FDI regimes proliferate and mature around the globe, governments are taking an ever-more expansive view of the concept of 'national security' to include more than military and defense interests, which means that FDI reviews are now easier to trigger than before," says Hrishi Hari, Dechert partner, Enforcement and Investigations (Washington D.C). "In the U.S., for example, it has been reported that the Committee on Foreign Investment in the United States (CFIUS) may block the acquisition of U.S. Steel by Nippon Steel, an investor from Japan (a staunch U.S. ally), over concerns regarding securing the supply of steel for the U.S. industrial base."

PE firms frequently find themselves caught in the crossfire from national security concerns – and many expect this to happen more often over the coming 12 months. Globally, more than half of respondents (51%) say increased foreign investment and national security scrutiny is likely to have a negative impact on their willingness or ability to do deals over the next 12 months.

For respondents in the Asia-Pacific region, where China's Foreign Investment Law, for example, presents tough challenges, the figure rises to 85%. In the EMEA region, 46% of respondents feel increased scrutiny will have a negative impact.

European policymakers continue to take a tougher line. Ireland, for example, is on the verge of introducing a new foreign investment regime, while the UK has made a series of interventions in cross-border deals, either referring them for review or vetoing them altogether. "The regulatory landscape for merger clearance in Europe has become more complex in recent years," warns York. "Alongside antitrust and FDI rules, PE investors need to be aware of the EU's new foreign subsidies regulation that can add a third layer of transaction conditionality."

By contrast, despite the high profile of CFIUS, PE firms in the U.S. appear to be less concerned. Only 40% of respondents in North America are worried about rising stringency from such regulators – and 29% think increased scrutiny of deals could have a positive impact on dealmaking. These may include, for example, U.S. firms that are intent on doing domestic deals, who may now see potential competitors being removed from the playing field.

"Given the heightened geopolitical tensions between the Five Eyes countries (Australia, Canada, New Zealand, the UK and U.S.) and adversaries like China and Russia, North American respondents are understandably more optimistic with respect to foreign investment scrutiny," says Hari. "Meanwhile, Asia-Pacific respondents, who are either in China or have indirect exposure to it, face a more challenging landscape."

> "Blowback on roll-ups from antitrust regulators is definitely on everybody's minds."
>
> 
>
> **Markus Bolsinger**
> Dechert LLP

Certainly, the Nippon Steel investment, and other deals that have been scuttled, feed worries that national security concerns are being commingled with protectionist agendas. However, savvy dealmakers appreciate the potential risk that FDI reviews add to transactions, and they are evaluating FDI risks early in the transaction process and deploying sophisticated strategies to manage potential risks.

Overall, greater scrutiny of foreign investment represents another headwind for the PE sector. At the least, concern that an otherwise potentially attractive transaction may run into regulatory trouble of this nature is likely to give dealmakers pause for thought. Non-domestic buyers may require more sophisticated strategies to navigate the transaction process while sellers may find themselves making their pitch to a reduced pool of bidders, undermining their exit strategy.

Co-investments: Best of both worlds?

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Co-investments can work well for GPs and LPs alike. "For the former, co-investment provides greater certainty of funding and helps mitigate the risk of funds becoming overly concentrated, particularly during periods when liquidity is at a premium," says Bolsinger. "For the latter, co-investments offer greater control over their exposure; the capability to deploy additional capital into the most attractive opportunities; the ability to make tactical allocations to attractive sectors or geographies; and the potential to secure more advantageous terms, possibly reducing their cost of capital."

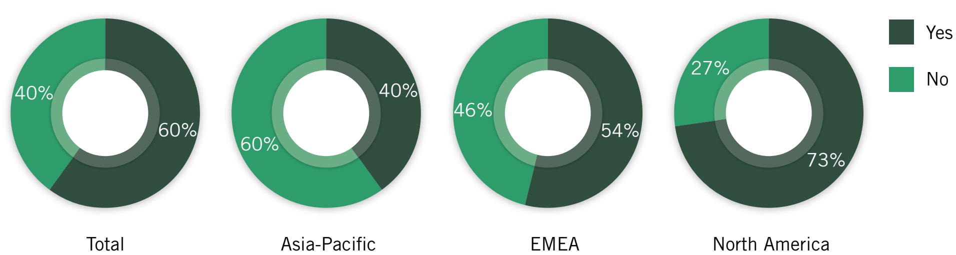
LPs are continuing to increase their commitments to co-investments, according to research from *Pitchbook*.

Our research reveals that co-investments are a popular strategy for firms, particularly those in North America. Overall, 60% of PE firms in our survey offer a co-investment program: that includes 73% of North American respondents, and 54% and 40% respectively in the EMEA and Asia-Pacific regions.

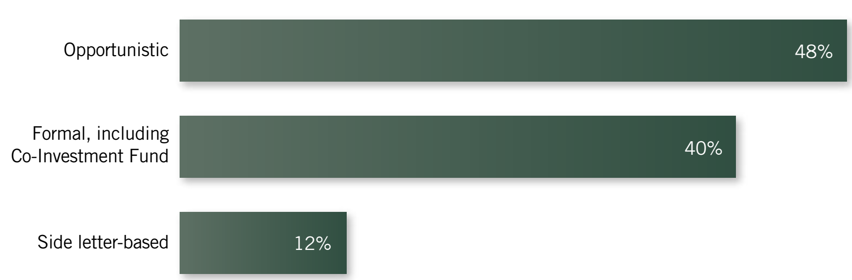
> If co-investment between GPs and LPs is increasing, one of the main questions will remain the fee structure – what will GPs ask LPs to bear?

Sabina Comis
Dechert LLP

DO YOU HAVE A CO-INVESTMENT PROGRAM?



IF YES, HOW IS YOUR CO-INVESTMENT PROGRAM STRUCTURED?*



*Question only given to those that have a co-investment program

The data chimes with advisors' experiences on the ground, says Comis. "We've seen a steady increase in the numbers of co-investment deals over the past three years," she says. "We see many more GPs looking to some of their LPs to invest in specific transactions."

The process must be managed carefully. GPs are conscious of the risk of misalignment, particularly where LPs are making the minimum investments required for access to a fund in order to secure significant exposure to direct deals; the effect can be to undermine the traditional relationship between GP and LP.

As for LPs, Comis warns: "In terms of risk profile, although co-investments technically offer greater control over the exposure and often more advantageous terms, they may also deprive the investor from the diversification protection offered by the manager providing averaged return."

That said, LPs are becoming more sophisticated, says Bolsinger, carrying out more of their own due diligence work to assess risk, and doing so at a pace that does not hold up the GP. He says: "LPs are now able to work within the transaction timeline, which was often a problem in the early days of co-investments, because you didn't know whether the LP would be there when you needed it."

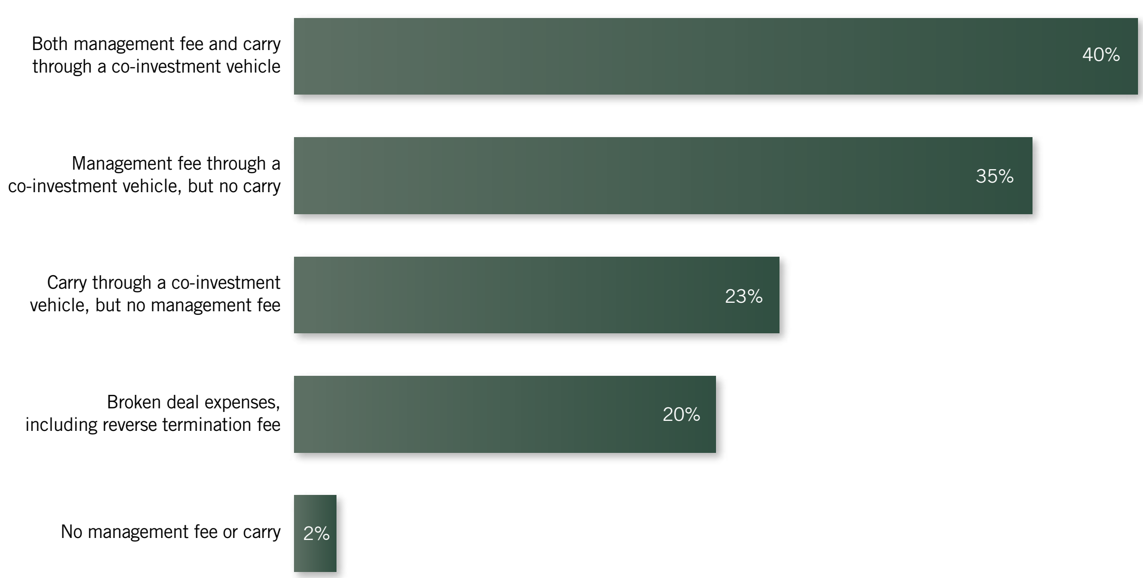
Indeed, from the LPs' perspective, co-investment brings certain due diligence advantages. Each allocation to a new PE fund requires its own diligence project, often necessitating a significant commitment of resources. But in a co-investment, the LP can deploy additional capital with a manager they have already vetted.

In practice, the nature of co-investment arrangements varies. In this research, of those firms that offer co-investments, just under half (48%) do so on an opportunistic basis, giving LPs ad hoc access to individual deals when they feel it is appropriate to do so. A further 40% offer more formal arrangements, such as co-investment funds, while 12% rely on side letter-based structures.

Diverse fee structures

One reason this distinction is important is that alternative types of arrangement generally come with different fee structures. "When co-investors are coming in deal by deal, they're typically not paying fees other than transaction costs, whereas in a fund, there are more likely to be management fees and carried interest," explains Bolsinger.

IF YES, WHAT FEES AND EXPENSES DO THE CO-INVESTORS BEAR/SHARE IN (SELECT ALL THAT APPLY)*



*Question only given to those that have a co-investment program

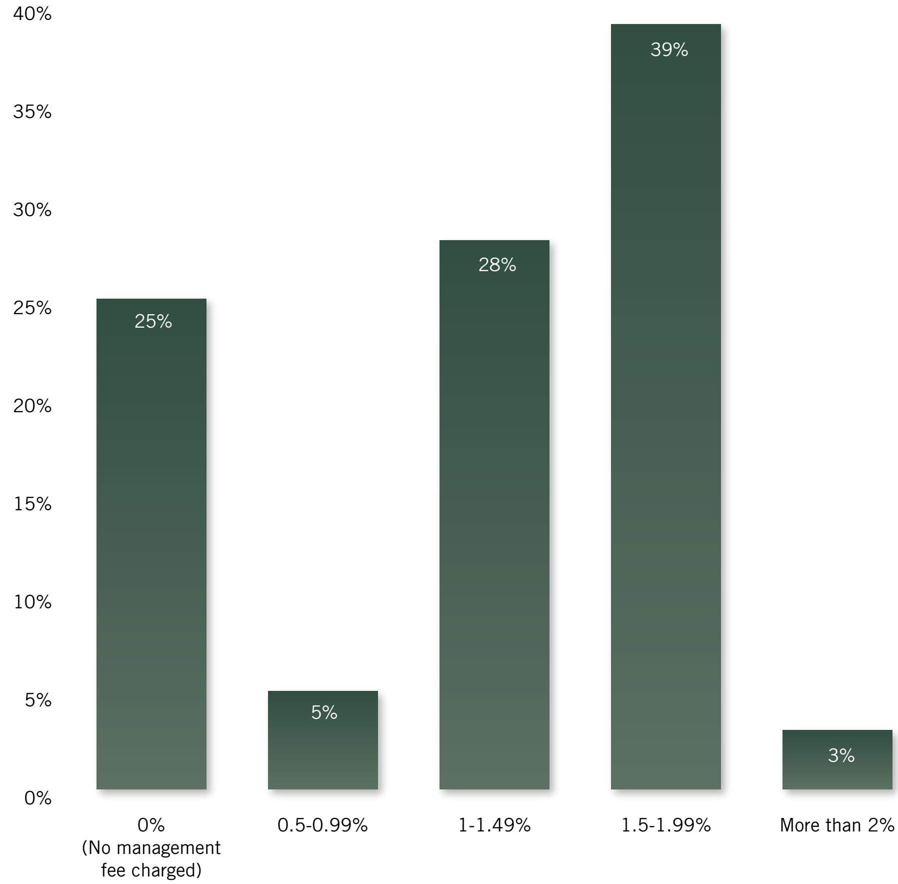
This is a live issue for PE with the approach still varying enormously across the industry. Of those firms offering co-investments, 40% levy both management fees and carry on their co-investment vehicle, with a further 58% levying one or the other.

Where firms do apply management fees on co-investment vehicles, two-thirds (67%) charge between 1% and 1.99% a year, while a quarter charges 0%. As for carry, the most common rate is between 10% and 15%, although more than a third (35%) charge no carry.

The onus is on GPs to get charging structures right, but there is an increasing determination to ensure that co-investments pay, says Comis. "The norms have changed, because in the past you would rarely see carried interest on a co-investment – the argument would be that you've already taken the carry on the main fund," she says. "By contrast, carry is now quite common on co-investment strategies – the question is how to find the right equilibrium in order not to make it too expensive for the market, so that LPs are still willing to come in."

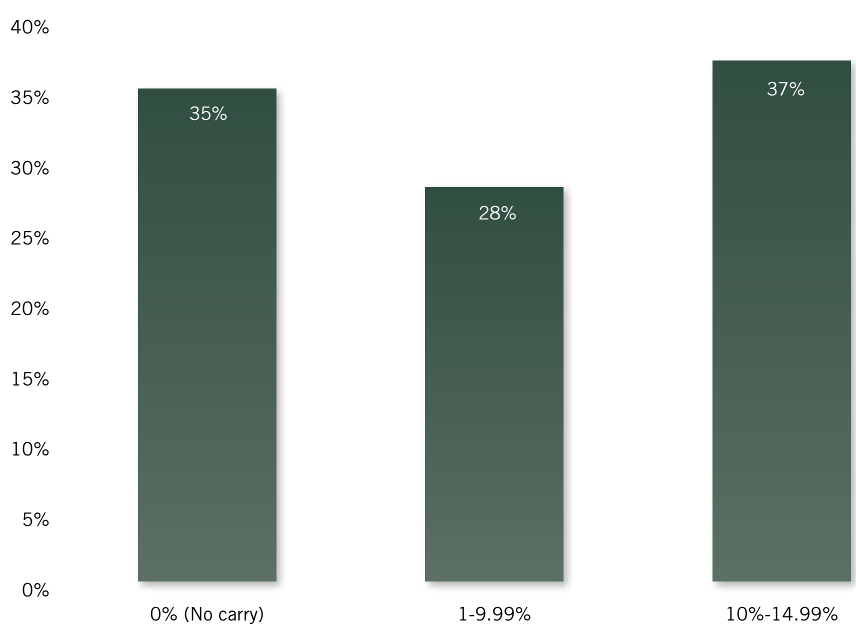
Naturally, there is room for compromise. Even where management fees and carry are payable on co-investments, the evidence from this research is that they tend to be set at lower levels than would be typical for a traditional PE fund. Just 3% of PE firms say they charge management fees of more than 2% on their co-investment vehicles; and none are demanding carry of more than 15%.

IF YES, WHAT, IF ANY, IS THE TYPICAL MANAGEMENT FEE APPLIED TO YOUR CO-INVESTORS THROUGH A CO-INVESTMENT VEHICLE?* (SELECT ONE)



*Question only given to those that have a co-investment program

IF YES, WHAT RANGE OF CARRIED, IF ANY, IS CHARGED TO LPS CO-INVEST?*



*Question only given to those that have a co-investment program

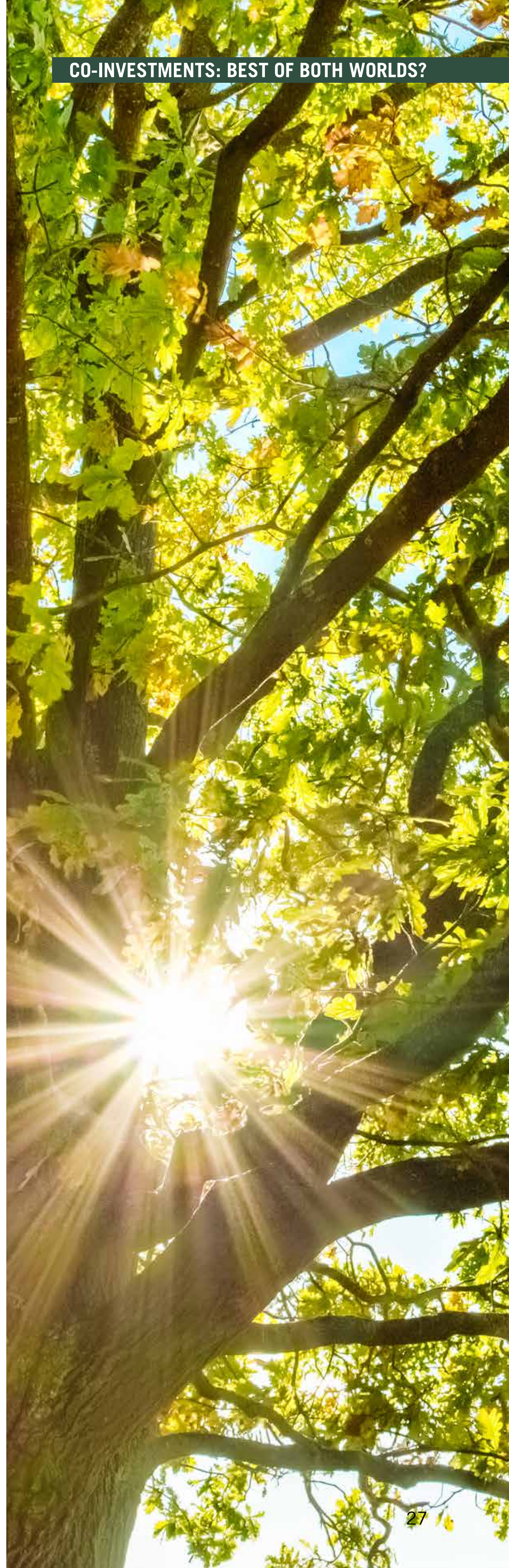
> With co-investors as partners, GPs can go after bigger targets, moving them into a smaller universe of competitors for these transactions.

Markus Bolsinger
Dechert LLP

Moreover, some LPs will clearly have more power than others. Where GPs are looking to raise co-investment funds from large and influential institutional investors, charging structures may be more competitive. Research from *Pitchbook* suggests large pension funds, for example, do not expect to pay any carried interest or management fees at all when participating in co-investment strategies.

To some extent, PE firms are still feeling their way here, suggests Bolsinger. “There is a back and forth, and there’s also a regulatory overlay where GPs cannot favor one LP over another without making all of the required disclosures around that,” he says. “But broadly, there is an expectation that charges are shared between the main fund and the co-investors.”

In the final analysis, the trend on charges will likely be determined by the underlying trend on co-investments. For as long as GPs are becoming more dependent on such vehicles, they will balance the need to attract LPs with the imperatives of maintaining fee income. Some may decide that the upside of co-investments – including access to larger and more attractive deals – is worth some sacrifice of income; others will be more focused on revenues.



North America **spotlight**

PE firms in North America made a solid start to 2024 and picked up further as the year progressed. That has given rise to increasing confidence that the sector can finish 2024 strongly and build into 2025.

There are several explanations for this shift. Most obviously, the practicality of bridging expectation gaps around valuations has been boosted by the prospect of looser monetary policy, as the U.S. Federal Reserve returns to a rate-cutting agenda. A definitive result in the U.S. presidential election campaign has also reduced domestic political volatility. And PE firms themselves are anxious to move forward after a tough period for exits and fundraising – 19 of the 25 firms globally with the largest amount of dry powder are U.S.-based, according to S&P Global.

"The mood is now one of optimism," says Bolsinger. "Some sectors are more positive than others, and the election impacted volume, if not value, in the third quarter, with people holding back some sales processes and were more hesitant about making acquisitions, but at least that uncertainty has now been resolved."

The data reveals the healthy state of the PE market in North America. Over the first three quarters of the year, PE deal values totaled US$382.3 billion, which represented a 49% increase on the same period in 2023. In volume terms, activity fell back only slightly, with the first nine months of the year seeing 2,664 deals, down 1% on the same period in 2023.

Some megadeals stand out. The US$10.2 billion acquisition of Endeavor Group in the leisure sector, for example, made headlines – not so much because of the nature of the acquiring consortium, led by Silver Lake, but because the business owns assets such as the Ultimate Fighting Championship (UFC) and World Wrestling Entertainment (WWE).

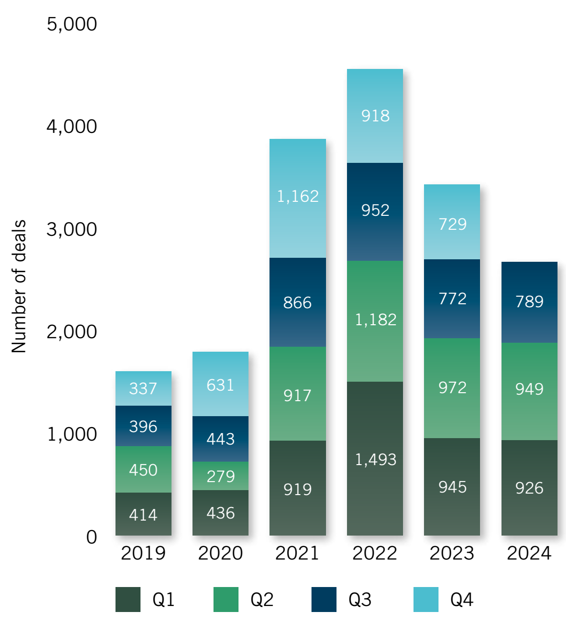
Sector watch

Much of the PE industry's activity during 2024 to date has been concentrated in a handful of sectors.

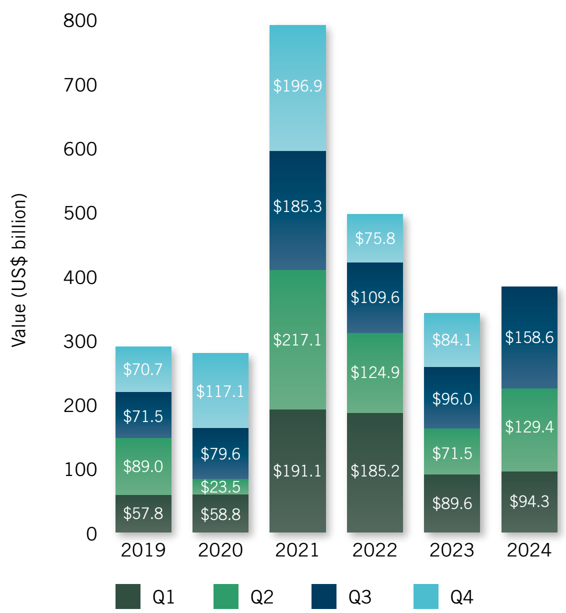
At the top of the list, the technology, media and telecoms (TMT) sector has seen US$179.5 billion worth of deals so far this year. Large buyouts included KKR's take-private acquisition of mdf commerce, a SaaS leader in digital commerce technologies in May 2024 and Silverlake and GIC's US$1.7 billion buyout of leading modern business monetization suite Zuora in October 2024.

This total figure for the TMT sector is up 67% from the US$107.7 billion of activity

NUMBER OF NORTH AMERICA BUYOUT DEALS, 2019–Q3 2024



VALUE OF NORTH AMERICA BUYOUT DEALS, 2019–Q3 2024



registered over the same period last year, with dealmaking now back at pre-pandemic levels.

North America's business services sector has also seen a spike in deal activity, with the total value of transactions seen over the year to date reaching US$27.2 billion, a 15% increase on the same period in 2023. That is largely due to a significant number of more modest deals, including Grant Thornton's sale of a majority stake of its advisory, tax, and consulting business to a consortium led by New Mountain Capital in March 2024.

Other sectors that have made a significant contribution to PE deal activity so far this year include pharmaceuticals, medical and biotechnology, with US$28.7 billion worth of transactions; industrials and chemicals, with US$24.7 billion; financial services, with US$31.8 billion; and leisure, with US$29.1 billion, more than double for the same period last year.

Real estate has also seen a noticeable spike in activity. This year, the sector has seen US$14 billion worth of transactions, up from US$3.6 billion in 2024, though much of the total was accounted for by a single transaction, Blackstone's US$9.4 billion acquisition of Apartment Income Real Estate Investment Trust.

The question for the industry now is whether the North American PE sector can continue on this upward path.

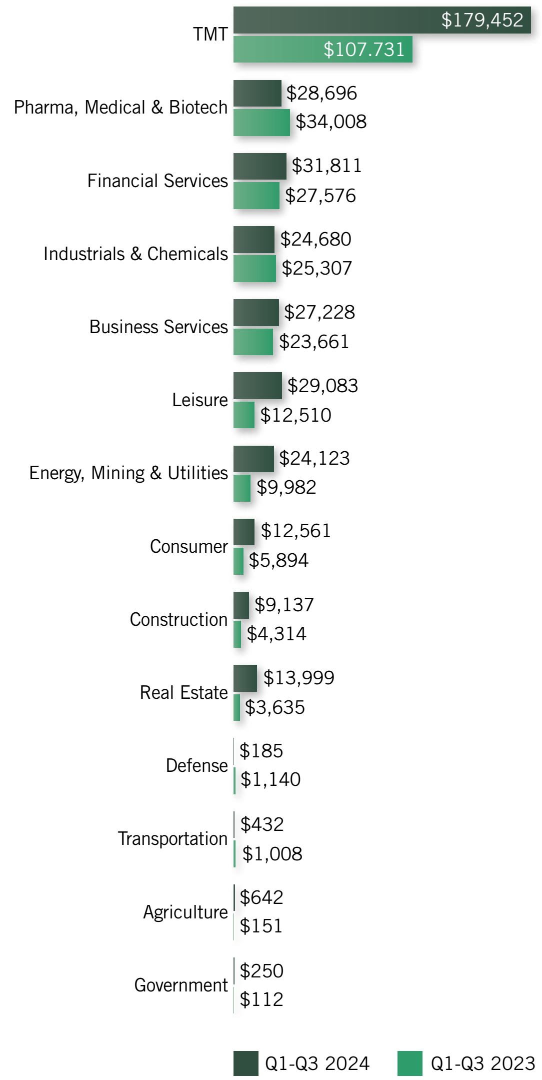
Bolsinger is hopeful. "What I think needs to happen, and hopefully will happen in 2025, is that the cycle continues to perform strongly, with more exits, more returns of capital to LPs, and then further commitments from LPs to new fundraisings," he says. "There are some encouraging signs that this cycle is now beginning to speed up."

Despite the upswing, the road to recovery will not be without challenges. A return to the ultra-low interest-rate environment that has characterized much of the past 15 years looks unlikely, despite interest rate cuts from the Fed.

And while politics may feel more settled in the U.S. itself, the international context is as challenging as ever, posing significant difficulties for the new administration.

Against this backdrop, dealmakers are confident that PE dealmaking activity in North America will continue to build – alongside a broader pick-up in activity such as fundraising.

PE BUYOUT VALUE BY SECTOR IN NORTH AMERICA (US$ MILLION), Q1-Q3 2024 VS Q1-Q3 2023



> It feels as if we were stuck in something of a wait-and-see holding pattern at the beginning of the year, but 2024 has begun to pick up, and there is momentum building that will lead us into next year.

Markus Bolsinger
Dechert LLP

Private credit

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The global private credit market continues to grow at pace, having quadrupled in size over the past decade to exceed the US$2 trillion mark for the first time in 2024, according to Preqin; with BlackRock predicting that figure could reach US$3.5 trillion by 2028.

Indeed, the growth of private credit has been so rapid that the IMF now fears the market may pose a risk to financial stability – it issued a warning earlier this year, urging regulators to be more proactive and intrusive in their supervision.

For PE firms, this rapid evolution of the private credit sector comes with certain ironies. On the one hand, it effectively represents a rival asset class from a fundraising perspective, providing investors with a different type of risk and return profile; some funding that might once have found its way into PE funds may now have been invested in private credit instead, particularly during "risk-off" periods for investors worldwide. On the other hand, the private credit sector provides a variety of new opportunities for PE firms to secure financing at both the portfolio and the fund level. Blackstone Alternative Credit Advisors, for instance, signed a US$5.5 billion multicurrency senior secured revolving credit facility, which is considered top of its class for the BDC industry; and Centerbridge Partners acted as co-lender on a US$510 million asset-based lending (ABS) transaction with Blue Owl, acting as collateral manager, and Société Générale, as arranger.

Meanwhile, KKR has worked on more than 25 individual financing transactions in the past year totaling over US$13.76 billion, including asset-based facilities, rated notes issuances, repurchase transactions and other innovative structures.

Indeed, PE firms attracted to the agility, speed and suitability of private credit products continue to make more use of the industry as the search for liquidity goes on. In our survey, firms worldwide highlight several areas in which private credit has supported their activities.

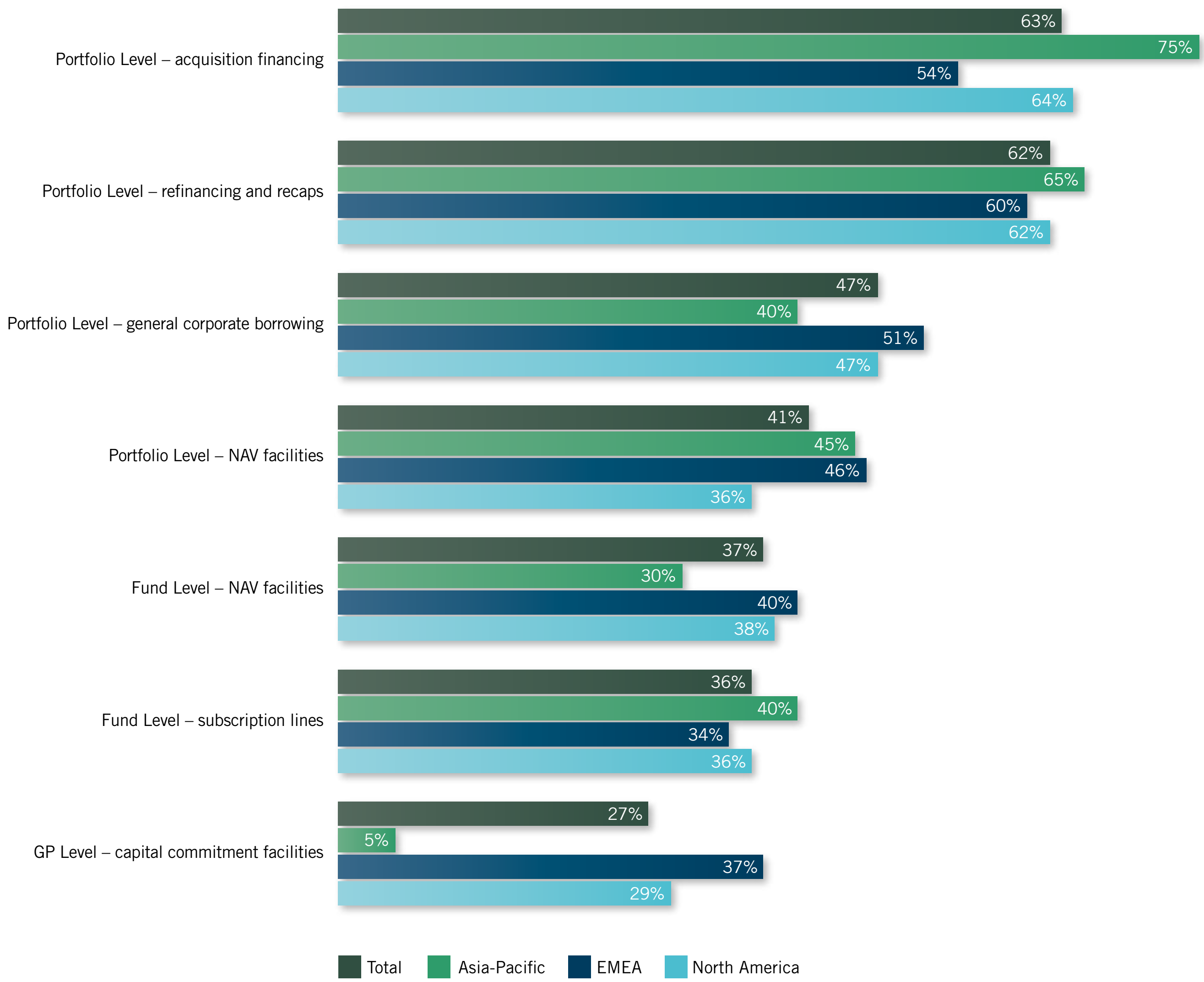
Most commonly, almost two-thirds of PE firms (63%) say they now use private credit to support acquisition financing in their portfolios; in the Asia-Pacific region, three-quarters of respondents cite this use case – perhaps surprising given the strong levels of bank liquidity available in the region for acquisitions, though India and Australia have seen significant private credit activity.

"The appetite for private credit remains strong across the product range currently being made available," says David Miles, Dechert co-head of global leveraged finance, corporate and securities (London). "With a hopefully reducing interest rate environment approaching and an improving M&A market, it will be interesting to see how private credit deploys relative to other financing solutions."

Private credit is also underpinning refinancings and recapitalizations, with 62% of PE firms worldwide using the sector's solutions in this way. More broadly, almost half of PE firms (47%) say they use private credit for general corporate borrowing at the portfolio level.

Net asset value (NAV) financing is another area in

WHERE IS YOUR FUND USING PRIVATE CREDIT? (SELECT ALL THAT APPLY)

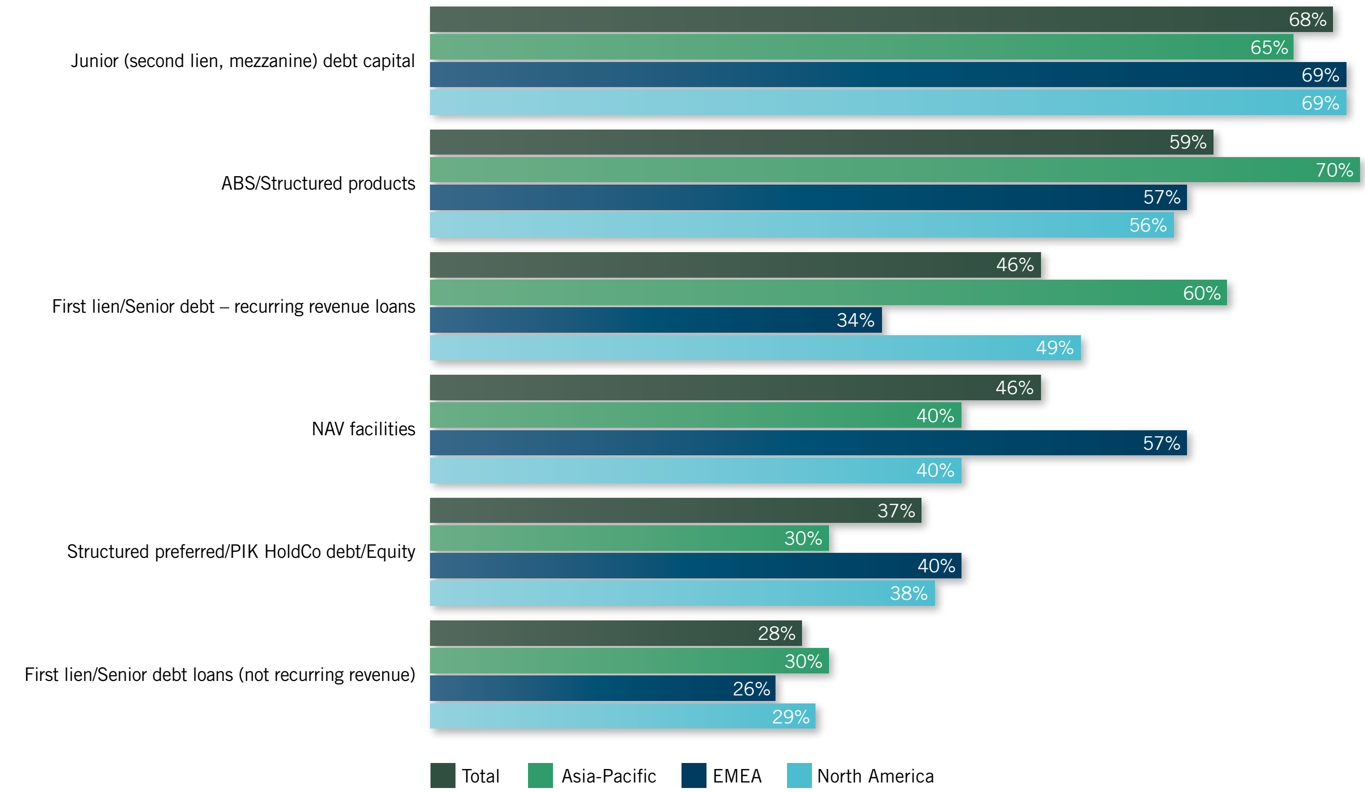


which the private credit sector continues to make inroads into PE firms, with significant minorities of funds taking on debt. Such facilities, involving loans secured against the net asset value of the underlying assets in their portfolios, provide GPs with a means to generate cashflow without having to turn to the secondary market. In the current environment, where the slowdown in exit activity has been marked, that functionality is particularly valuable, enabling firms to return cash to investors. Texas-based Vista Equity Partners and Sweden's Nordic Capital are among those to have used NAV financing this year.

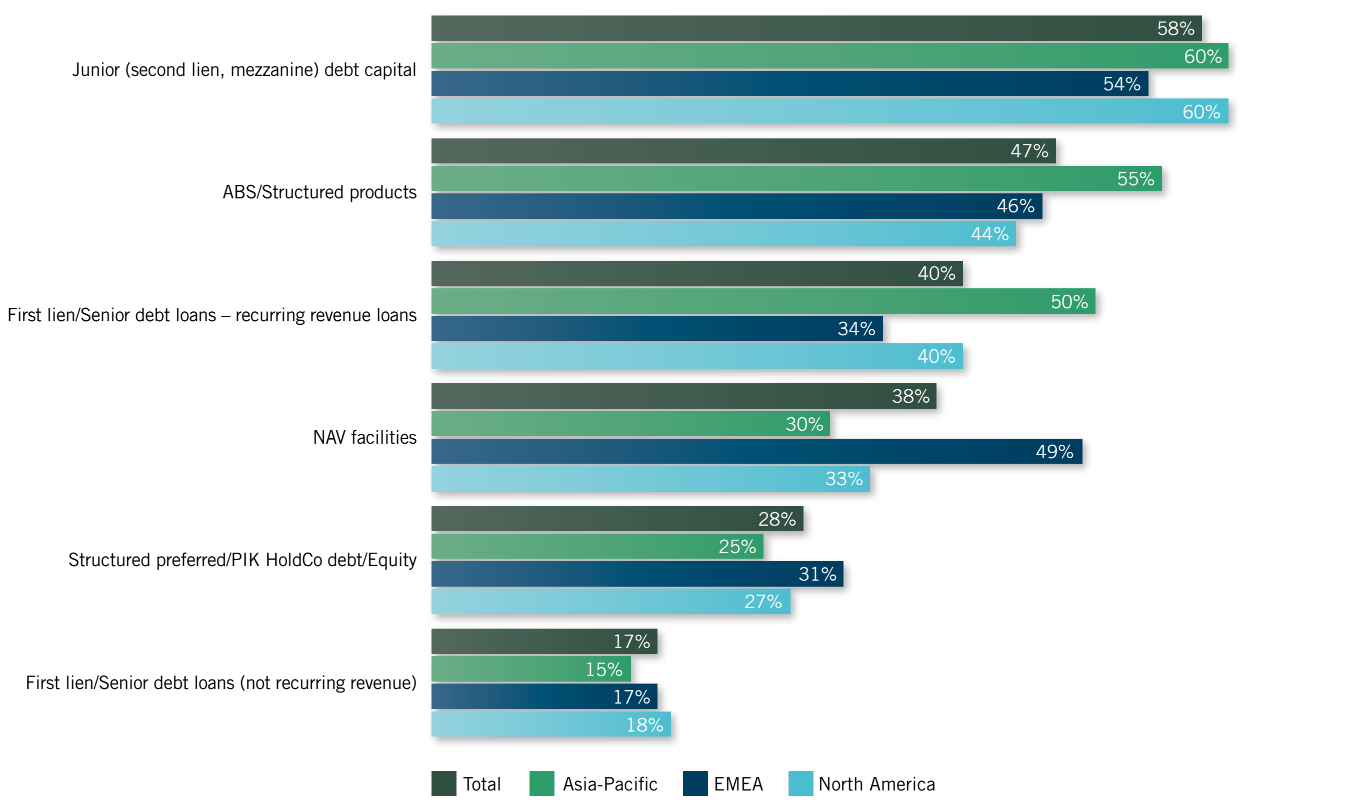
Similarly, more than a third of PE firms in this research (36%) say they have set up subscription lines. These are loans secured against the commitments to the fund made by investors – rather than on the underlying assets – and help the GP to manage capital calls on LPs more efficiently and LPs to manage their own funding requirements. The added advantage is that by shortening the holding period for investors' capital, the internal rate of return (IRR) on investments that appreciate in value will naturally be higher (but cash-on-cash return will be lower).

However, in a falling interest-rate environment, it may be that private credit investors are inclined to divert their allocations to other capital strategies, including PE, warns Bolsinger.

WHICH OF THE FOLLOWING TYPES OF PRODUCT DOES YOUR FIRM USE IN PRIVATE CREDIT? (SELECT ALL THAT APPLY)



AND OF THESE TYPES OF PRODUCT, WHICH DO YOU EXPECT YOUR FIRM TO USE WITH INCREASING FREQUENCY OVER THE NEXT 12 MONTHS? (SELECT ALL THAT APPLY)



"If rates are coming down, we may see private credit cool a little bit," he says. "These lenders have wedged themselves into the space where the banks used to be before they retreated, and I don't think that's going to change. I do think, however, you will see banks trying to get into the private credit market, as Wells Fargo did when it partnered with Centerbridge."

Debt instruments

For now, PE firms are continuing to avail themselves of a broad range of debt instruments.

Junior debt, senior debt, NAV facilities and asset-backed securities (ABS) are all commonly held by respondents – though there are some nuances by region.

For example, firms based in Asia-Pacific are more likely to say they use ABS and other structured products than their counterparts in the EMEA region and in North America, respectively. They are also more likely than their international counterparts to hold first lien or senior debt. Firms based in the EMEA region are the most likely to be using NAV facilities.

Looking ahead, many PE firms are clearly expecting to continue to work closely with providers – and to do so across a variety of debt products.

In particular, 58% of PE firms taking part in this research say they will use junior debt facilities more frequently over the next 12 months; 47% expect to make more use of the ABS market. Again, Asia-Pacific-based firms are particularly likely to explore this latter solution.

Elsewhere, it is notable that 49% of EMEA-based PE firms are expecting to increase their use of NAV facilities. Among North American firms, meanwhile, 40% anticipate increased use of first lien and senior debt loans.

All of which suggests that the wide range of solutions that private credit providers can offer will continue to appeal to their peers in the PE industry. Further regulatory scrutiny of private credit might skew this picture over time – as might a decline in availability if interest rates continue to fall – but significant numbers of firms believe private credit offers value in current market conditions.

"Private credit has shown that it is able to lend at scale across sectors, with multiple product ranges providing flexibility of solutions to particular transactions and very often with single counterparty execution risk," says Miles. "Those features, in a market where, at times, other financing solutions have not been as available due to broader macroeconomic conditions or other broader restrictions, has enabled private credit to continue to grow its share of the lending market space in many geographies."

EMEA **spotlight**

Dealmaking has remained consistent in the EMEA region, with value, if not volume, showing a solid increase. Over the first three quarters of the year, the region saw 2,458 deals worth a total of US$203.7 billion, compared to 2,574 deals worth US$119.0 billion over the same period in 2023.

And despite the decrease in volume, activity in the EMEA region remains well ahead of pre-pandemic levels. In 2019, for example, there were 1,236 deals recorded over the first nine months of the year – around half the number seen during the first three quarters of 2024. Indeed, this year has already seen significantly more transactions than the whole of 2019.

And after a slow start to the year, exit activity is beginning to rise. For example, *Pitchbook* reports that the EMEA region saw exit values surge by 90% in the second quarter of the year after a relatively slow start to the year. There has also been a pick-up in the number of larger transactions, with 46 deals worth more than US$1 billion between Q1 and Q3 2024. A more supportive economic background also holds promise, with central bank policymakers having moved to loosen monetary policy.

Expect the unexpected

However, dealmaking is unlikely to bounce back to the outlier levels seen in 2021 and early 2022, according to Field. The economic outlook for the region is far from bright with the IMF currently predicting GDP growth of just 1.5% in both the UK and the eurozone during 2025, albeit up from 0.1% and 0.5% respectively this year; and there is an uncertain geopolitical outlook.

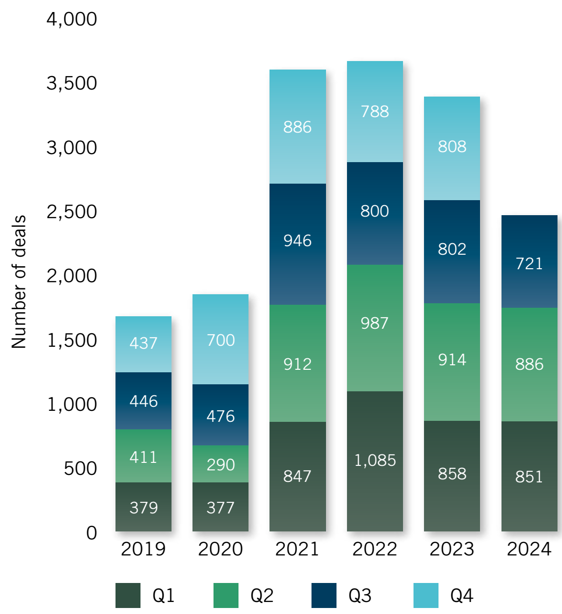
"Next year should be stronger, but the one thing we've learned over the past few years is that politics trumps economics," says Field. "Almost nobody foresaw Russia's invasion of Ukraine or Hamas' attacks on Israel, but the consequences of the unexpected are huge."

Sector watch

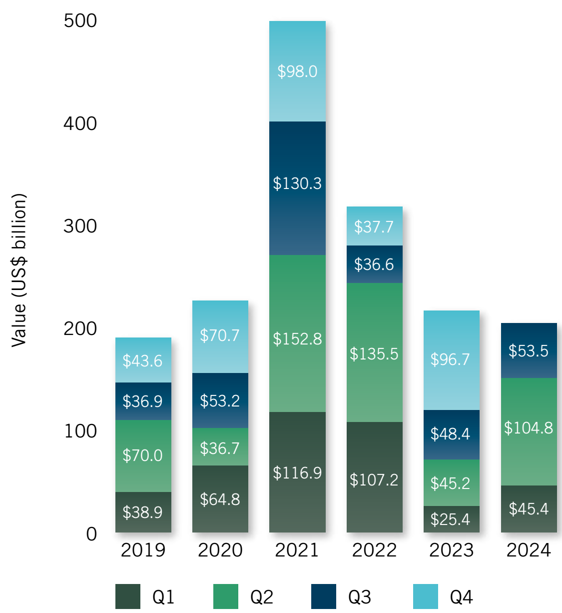
On a sectoral level, deal value has increased across the majority of sectors.

For example, technology, media and telecoms (TMT) remains the busiest area of the deal market for PE firms, recording US$75.4 billion worth of transactions during the first nine months of the year, more than double last year's total of US$35.2 billion. The biggest deal of the year so far has been Apollo Global Management's 49% stake purchase of Intel Corp (joint venture entity related to Fab 34), based in the Republic of Ireland, for US$11.0 billion.

NUMBER OF EMEA BUYOUT DEALS, 2019–Q3 2024



VALUE OF EMEA BUYOUT DEALS, 2019–Q3 2024



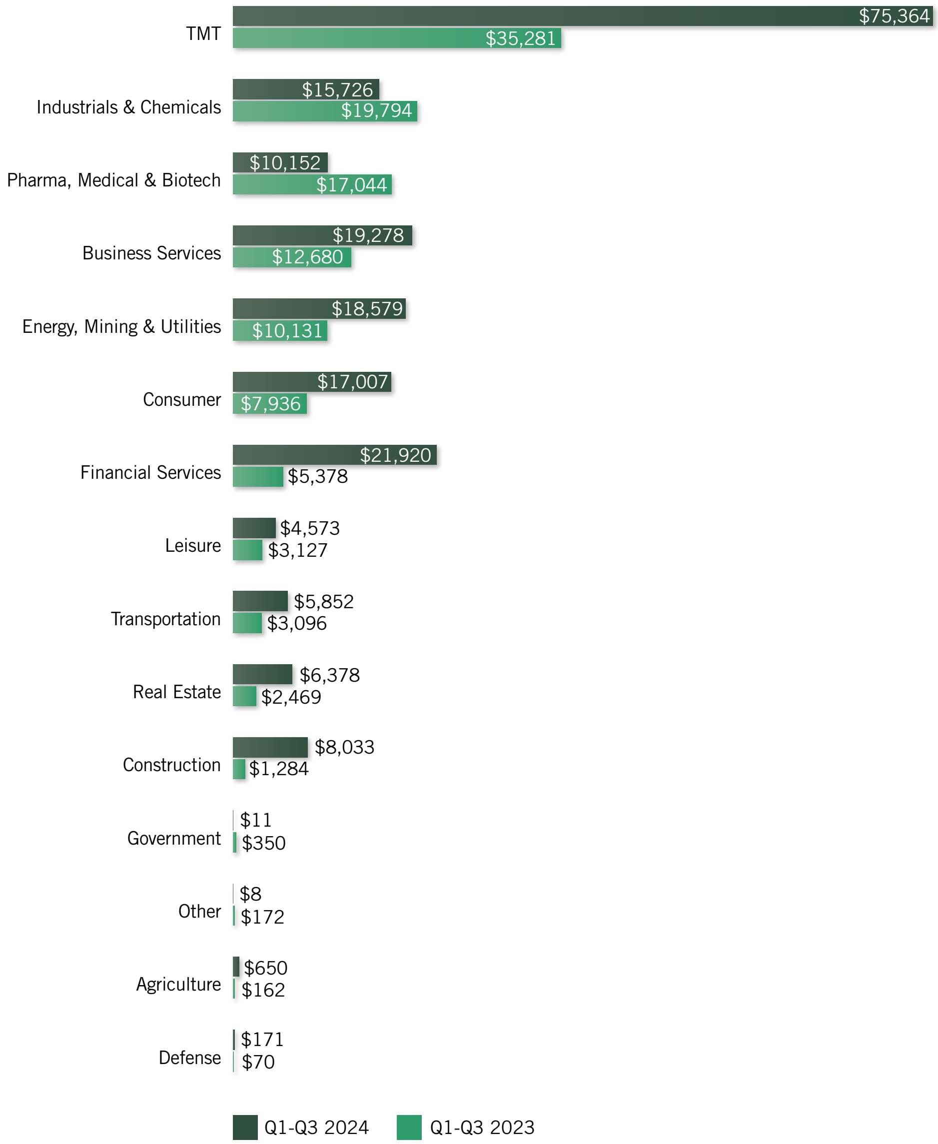
Deal value in the financial services sector has also performed impressively. The industry saw US$21.9 billion of transactions during the first three quarters, eclipsing Q1-Q3 2023's total of US$5.4 billion. Standout deals include a buyout announced by a consortium including CVC Capital Partners in the second quarter to acquire the UK investment platform Hargreaves Lansdown for US$6.7 billion.

That deal is the latest in a series of take-private transactions that have continued in the EMEA region this year – a 2024 study for the Centre for Private Equity and MBO Research found that the proportion of buyout activity accounted for by such deals has increased threefold compared to 2023. See *Part 8: Deal Trends* for more on take-private transactions – and how stronger stock markets may be leading to a pullback from this kind of deal.

Business services, the third busiest sector in deal value terms, saw transactions worth US$19.3 billion during the first three quarters of the year. This was considerably up from last year's first-half total of US$12.7 billion.

The consumer sector also saw a wealth of activity. PE firms were involved in deals worth US$17.0 billion over the first nine months of the year, up from US$7.9 billion in the same period last year – an increase of 114%. The largest deal of the year so far saw PAI Partners acquire UK-based Auditonix Holding for US$2.5 billion.

PE BUYOUT VALUE BY SECTOR IN EMEA (US$ MILLION), Q1-Q3 2022 VS Q1-Q3 2023



> "We are not going to match 2021, but as long as there are no more nasty surprises, the outlook for 2025 is much more positive."

Chris Field
Dechert LLP

Deal trends

Dechert contributors

Dean Collins
Singapore

Maria Tan Pedersen
Singapore

In a marketplace where investors have been somewhat risk-averse, many PE firms are focusing on mitigation and protection, and our research reflects this trend.

Most strikingly, 61% of PE firms say that club deals are very appealing in the current environment. A practice that has traditionally enabled GPs to acquire larger companies than they could target alone – still useful in an era of limited liquidity and challenges to fundraising – also provides risk mitigation benefits, requiring smaller stakes in individual companies.

One notable club deal this year was GIC's acquisition of a 25% minority stake in Reworld, a provider of sustainable waste solutions, from EQT Infrastructure V fund in October.

"People have been cautious," notes Field. "The economic data has been mixed, and there has been fear of a recession – so while firms know they need to be doing deals, they also want some downside protection and club deals allow them to lay off at least some risk.

"It's also reassuring to know that other investors have run due diligence on a particular investment and reached the same conclusions about its value."

Other risk mitigation tactics are also to the fore. For example, almost half of PE firms (48%) say they are diversifying their fund strategies, while 41% cite their interest in working with strategic partners. And while only 23% of firms say they are very likely to consider co-investment opportunities, a further 38% describe themselves as open to the idea.

"Often, it's not only about money but also about specific expertise or other competencies that people bring to the table in club deals and similar arrangements," says Bolsinger. "There are risks, particularly with governance and oversight if a deal begins to go sideways, but these can be managed."

> "Club deals are helping PE firms to both diversify risk a little and to manage those very large checks."
>
> 
>
> **Markus Bolsinger**
> Dechert LLP

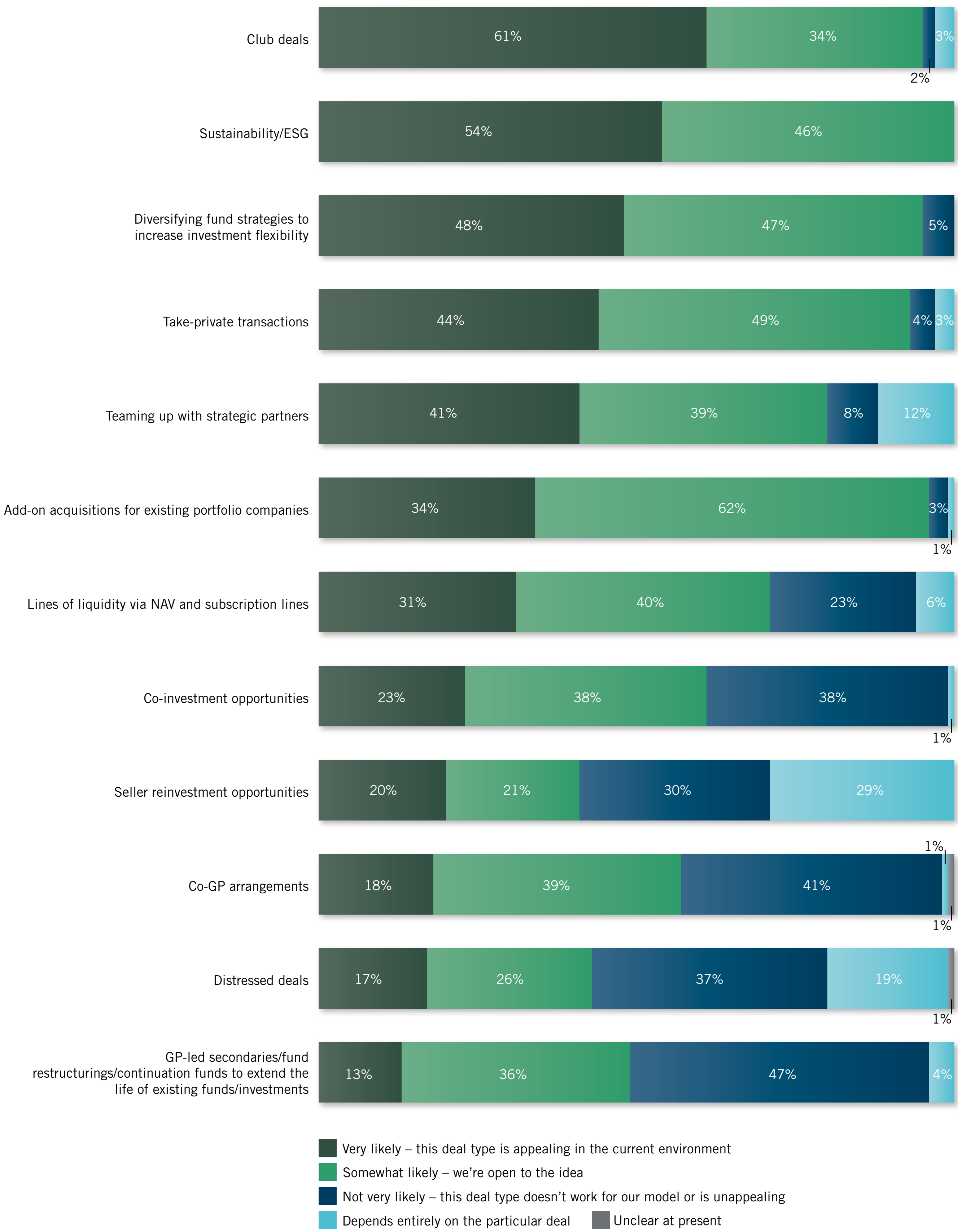
Could take-privates be on the wane?

Other notable deal trends here include a decline in overall enthusiasm for take-private transactions. These were the top deal type being considered by firms last year, with 80% very likely to undertake such a transaction and 14% somewhat likely.

That fervor for take-privates has been tempered this year – although 93% of respondents overall note that they are likely (either very or somewhat) to consider a take-private, the percentage of those in the 'very likely' group has fallen to 44%.

Part of the story is that take-private deals have become more expensive – despite volatility, 2024 has been a strong one for most global stock markets, with exchanges in the U.S. up by more than 10% and most European and APAC markets also tracking higher. "The public to private

HOW LIKELY IS YOUR FIRM TO CONSIDER THE FOLLOWING DEAL TYPES AT PRESENT? (SELECT ONE FOR EACH TYPE)



market valuation differential is narrowing," says Field. "That concentrates PE firms' minds on the reality that take-private deals are much harder work, with greater execution risk and the potential for reputational or additional regulatory issues."

However, Bolsinger expects at least some activity in this area to continue. "Much of the performance of the U.S. market has been down to the 'Magnificent Seven' technology companies but many of the remaining 493 companies are still not performing strongly," he points out. "So, while the very low hanging fruit may have been taken, there is still interest in taking attractively valued companies private."

Indeed, despite the relative reticence of respondents about the likelihood of future take-privates, the number of deals in 2024 looks set to surpass 2023 and there have been several mega take-privates, particularly in the U.S. These include the recent club deal acquisition of Smartsheet, the project management software company, for which Vista Equity Partners and Blackstone paid US$8.4 billon.

It is also worth noting that every single respondent in this research is considering undertaking sustainability and environmental, social and governance (ESG) investment deals. While there has been much debate about ESG investment over the past year, particularly in the context of a backlash against this approach in the U.S., it's clear that PE firms have no intention of walking away from this area. In the EMEA region, for example, PwC expects three-quarters of European funds to be ESG-themed by 2027. See *Part 10: Sustainability and ESG* for more.

Asset class assessment

In terms of asset class allocation in the next 24 months, firms are currently exploring multiple areas of interest.

At the top of the rankings, three-quarters of PE firms (75%) say they are considering investing in venture capital over the next two years. This might feel counter-intuitive given the generally risk-averse mood across most firms right now, though the risk-off environment of the past year or two has seen asset values fall, increasing the opportunistic attractions of early-stage investing.

In addition, Collins points to the strong long-term track record of the asset class. "There have been some great exits and some off-the-chart returns from venture capital," he points out. "It has been tougher in the Asia-Pacific region over the past couple of years, particularly on exits, but blockbuster valuations have certainly attracted investors."

Infrastructure, meanwhile, feels more appropriate to the prevailing market conditions, given the income thrown off by many assets – often inflation-backed – and the physicality of the asset class. "Infrastructure provides the long-term, stable returns that so many people are looking for right now," says Bolsinger.

In this context, almost two-thirds of PE firms in this research (65%) say they are considering making investments in infrastructure over the next two years, up from 40% who said the same in 2023. Indeed, PE has been a driving force in the growth of infrastructure in recent times, a trend dubbed as a shift from "investment backwater to a US$1 trillion asset class" by the *Financial Times*.

"Investors are excited about drivers such as population growth, particularly in markets like India and Indonesia," adds Pedersen. "There's also huge hype around energy transition and investment in renewable energy infrastructure; nor should the opportunities in digital infrastructure – fiber optic networks and data centers, for example – be overlooked."

Several other asset classes are also experiencing significant increases in demand compared to a year ago.

> Take-private deals benefitted from the fact that many markets were very down; that's no longer the case.

Chris Field
Dechert LLP

> Infrastructure is hot – and that includes digital infrastructure, where the interest is huge.

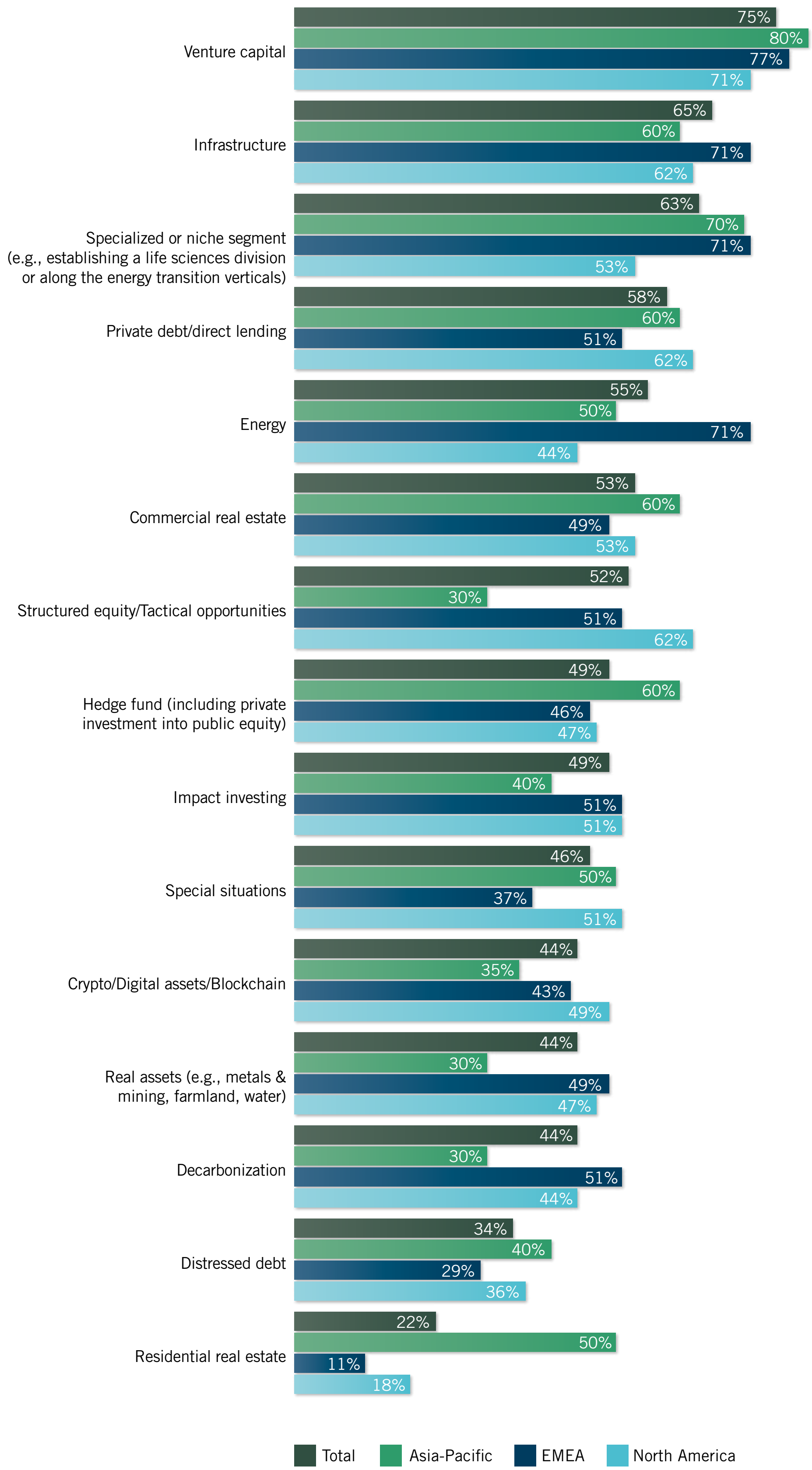
Maria Tan Pedersen
Dechert LLP

More than half of the PE firms in this research (55%) are considering energy, compared to only 30% in 2023, another example of the increasing interest in infrastructure and infrastructure-adjacent asset classes; 58% say they are interested in private debt or direct lending, up from 30% a year ago.

Naturally, there are also significant regional variations. For example, energy is a notably more popular asset class for firms based in EMEA, with 71% looking at potential investments. Asia-Pacific PE firms are more likely to be interested in hedge funds (cited by 60%) and residential real estate (50%) than their peers elsewhere. And in North America, structured equity (62%) and digital assets (49%) are stand-out areas of difference.

In addition, almost two-thirds of PE firms (63%) say they are considering investing in a specialist or niche segment of the market. This could be anything from a life sciences specialty to a focus on decarbonization. Specialist funds look set to proliferate as GPs seek new sources of competitive differentiation in their appeal to LPs. Indeed, according to the Mantra Niche PE Index, which tracks average returns on a rolling ten-year basis, niche or specialist PE has generated an average annual return of 42% over ten years, outpacing the overall 21% average annual return by a factor of two.

WHICH OF THE FOLLOWING ASSET CLASSES IS YOUR FIRM CONSIDERING INVESTING IN OVER THE NEXT 24 MONTHS? (SELECT ALL THAT APPLY)



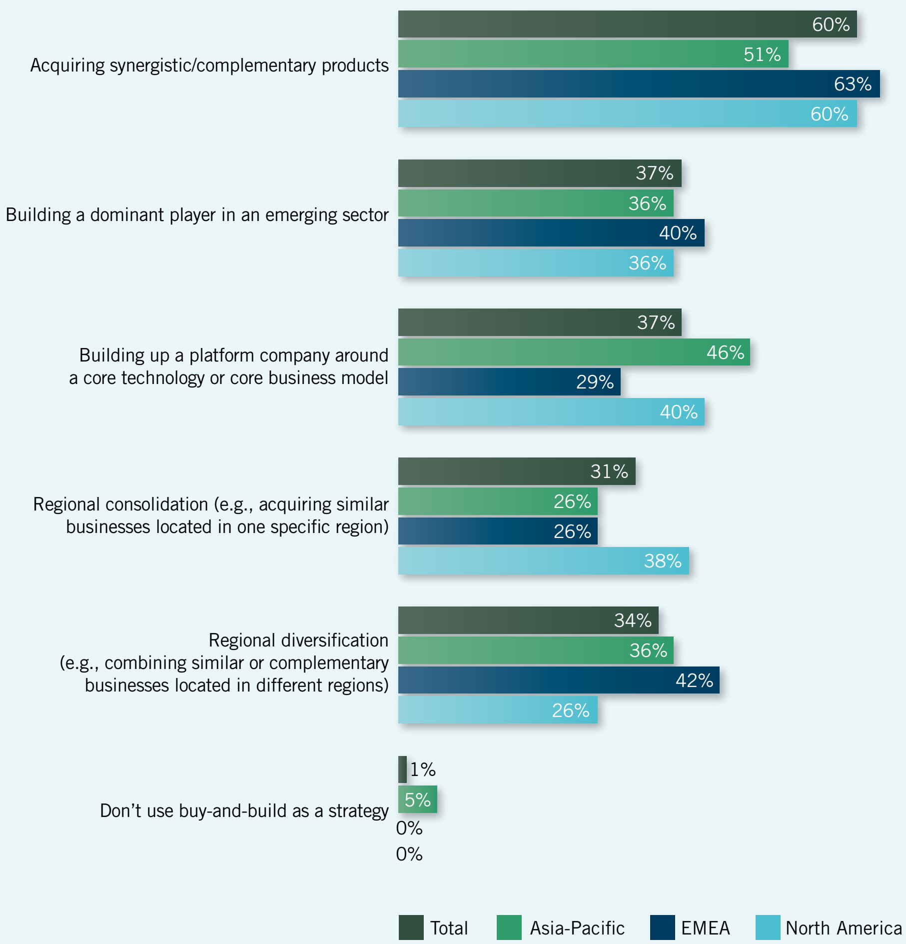
Buy and build: Toward new approaches

Buy and build remains a key strategy for most PE firms. In the first quarter of the year, more than half of all deals in some regions were bolt-ons, DC Advisory reports. However, approaches to buy and build vary – and naturally change over time. In last year's research, firms were most likely to say their preferred approach to buy and build was to identify an emerging sector and then to build a dominant player in that industry. This year, by contrast, more PE firms are focused on acquiring synergistic or complementary products to drive their buy-and-build strategy forwards.

In each region, more than half of respondents say this strategy is the one they use most often. Worldwide, 60% of PE firms regard this route as a key plank of their buy-and-build strategy, compared to 37% focused on the emerging sector route.

Other preferences for buy-and-build strategies, by contrast, vary significantly by region. The platform approach, for example, is favored particularly strongly by firms based in the Asia-Pacific region and, to a lesser extent, in North America. Firms based in EMEA are particularly likely to be focused on regional diversification,

WHICH BUY-AND-BUILD STRATEGIES DO YOU CURRENTLY USE MOST OFTEN? (SELECT TOP TWO)



while their North American counterparts stress the value of regional consolidation.

This is not to suggest that buy and build is always straightforward. The ongoing imperative to keep making acquisitions is demanding, with PE firms simultaneously required to identify new targets, manage deal processes, oversee integration and monitor performance.

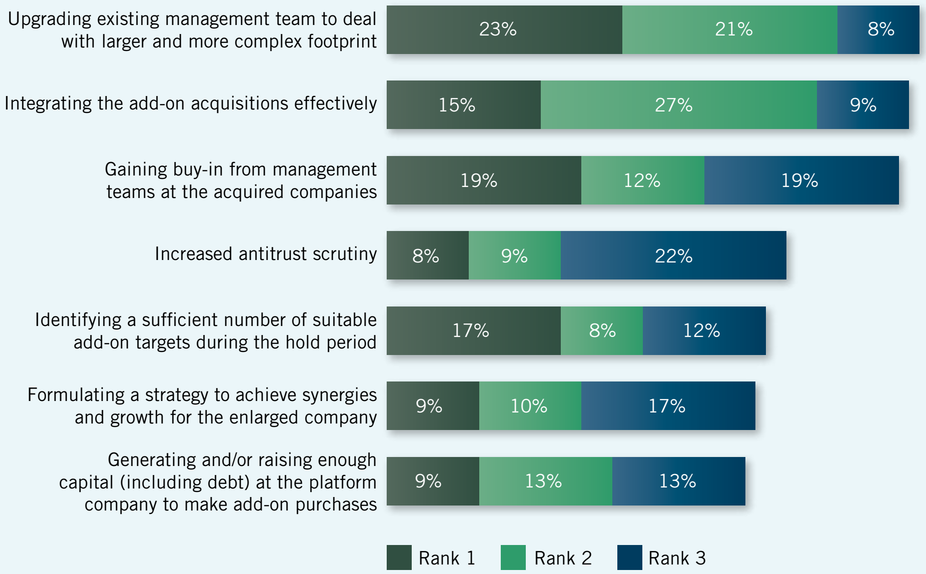
PE firms are acutely aware of the need to manage growing pains as the buy-and-build strategy gathers pace. More than half of respondents (52%) point to the challenge of upgrading the management team of the business as it expands and potentially extends its footprint. Almost as many (51%) single out the difficulties of effective integration of bolt-on acquisitions.

It can also be challenging to maintain the support of companies acquired as part of the buy-and-build process. Half of PE firms (50%) say they find it difficult to get buy-in from the management teams of these companies.

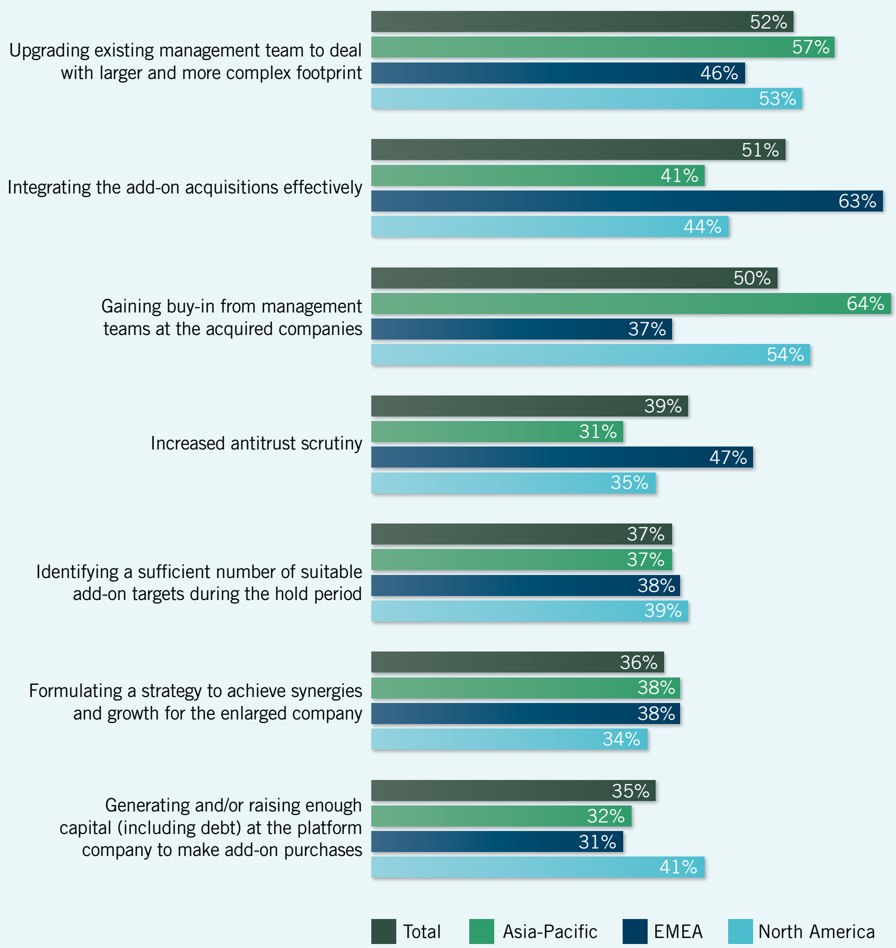
PE firms in different regions are challenged in different ways. While respondents worldwide agree on the difficulties of integration and management, firms in the EMEA region are held back by antitrust concerns, with 47% citing this as a potential issue. In North America, meanwhile, firms are particularly likely to worry about how to raise sufficient capital at the platform company to make add-on purchases; 41% point to this issue.

Asia-Pacific-based firms are less likely to single out other challenges, but they are more likely to be struggling to gain management approval. Almost two-thirds of these firms (64%) say it is difficult to get buy-in from management teams when they make new acquisitions.

WHAT ARE THE BIGGEST CHALLENGES YOUR FIRM FACES WHEN MAKING ADD-ON ACQUISITIONS FOR A PLATFORM COMPANY? (SELECT TOP THREE AND RANK 1-2-3, WHERE 1 IS MOST IMPORTANT)



WHAT ARE THE BIGGEST CHALLENGES YOUR FIRM FACES WHEN MAKING ADD-ON ACQUISITIONS FOR A PLATFORM COMPANY? (SELECT TOP THREE)



Asia-Pacific **spotlight**

Given the headwinds that have blown into the region, particularly China's economic downturn in the past year, PE activity has been remarkably resilient in the first nine months of 2024.

In value terms, the first three quarters of 2024 saw the region record US$113.8 billion worth of deals, compared to the US$99.4 billion seen during the same period in 2023. While this does not match the highs of 2021, the latest figures far surpass the pre-pandemic deal values typical for the Asia-Pacific region.

The data looks just as resilient in volume terms. Over the year so far, there have been 1,756 transactions – 5% up on the 2023 figure of 1,676, and well ahead of the pre-pandemic years as well as 2021.

"It's certainly been active, but maybe not as active as some people expected," says Collins. "Valuation expectations didn't moderate in quite the way that people thought, with sellers deciding to wait or to explore different kinds of deals, and buyers reluctant to overpay."

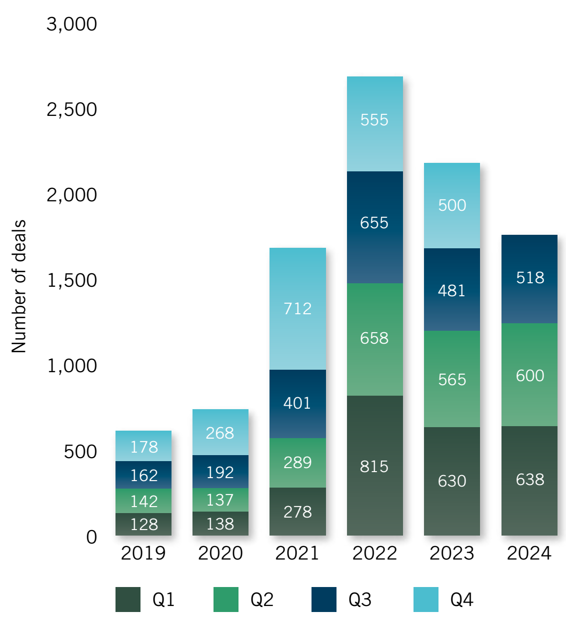
Still, in a large and diverse region, it's important to recognize that the overall figures mask significant variations. Data from China, for example, shows that deal activity has slowed in 2024; in the first nine months of the year, dealmakers in China did 466 deals worth US$29.4 billion – compared to 470 deals worth US$31.1 billion in the same period in 2023. India, by contrast, was more of a bright spot. It recorded 276 deals over the first three quarters of the year, up from 246 in 2023.

In Southeast Asia, activity has also picked up after a slow start to the year. Between Q1 and Q3 2024, deal value stood at US$8.8 billion, almost double the US$4.6 billion recorded for the same period last year.

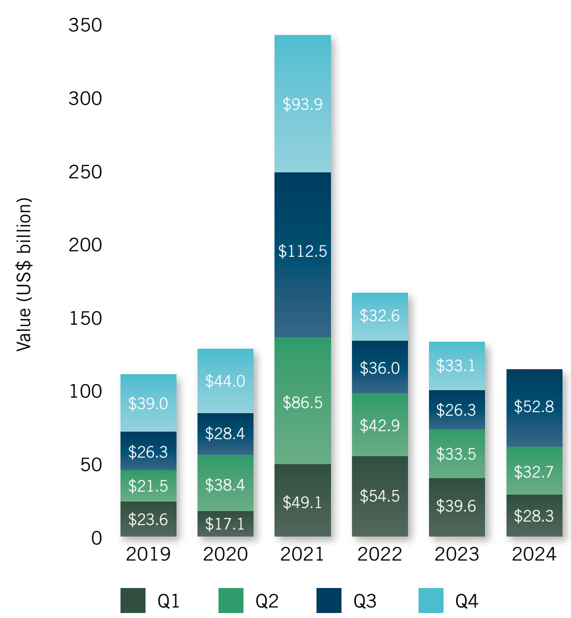
Indeed, Southeast Asia could become a particular focus for the PE sector, with good levels of dry powder across the Asia-Pacific region finding its way into markets such as Indonesia, Vietnam and the Philippines, where firms have often been less active in the past. Singapore, meanwhile, also continues to attract attention.

The industry is adjusting to evolving market conditions, including concern over China's economic challenges, says Pedersen. "China is still the largest economy in Asia, but there are reasons why people don't invest in China," she says. "It may be that we now see more regional funds – vehicles that focus more tightly on markets other than China – in India, Southeast Asia or elsewhere."

NUMBER OF ASIA-PACIFIC BUYOUT DEALS, 2019–Q3 2024



VALUE OF ASIA-PACIFIC BUYOUT DEALS, 2019–Q3 2024



Sector watch

On a sectoral level, the majority of industries saw an uplift in deal value. Real estate saw the largest percentage increase in the total value of deals recorded over the first three quarters of the year, with figures more than quadrupling year-on-year to US$12.3 billion. Data from Preqin identifies Japan – and particularly office accommodation in Tokyo – as a particular area of interest for investors during the first half of the year.

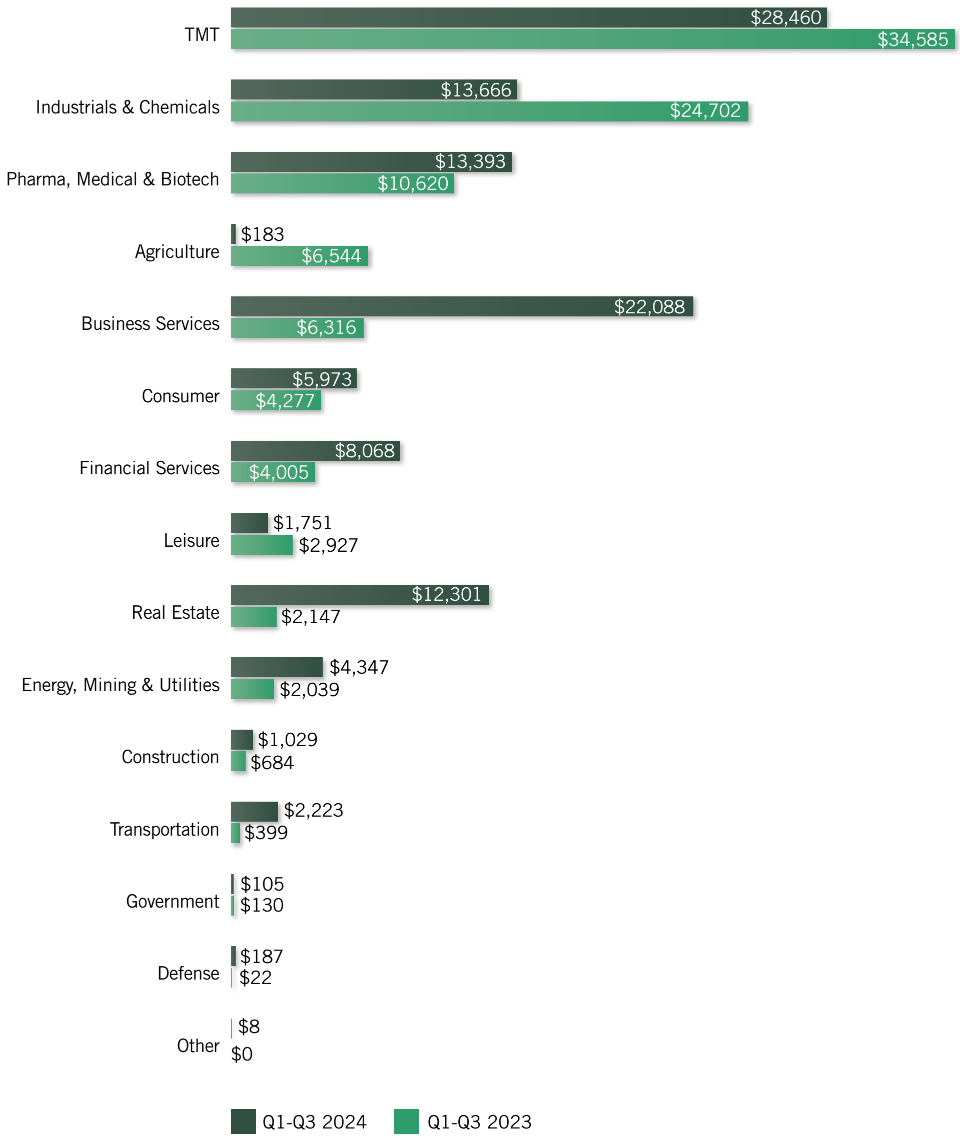
The TMT sector has been the most active part of the market so far this year, with PE firms completing US$28.5 billion worth of buyouts to date. However, this figure is down 18% on the US$34.6 billion recorded at the same stage of 2023.

Sectors that saw significant value increases include business services, which recorded US$22.0 billion worth of deals – up 250% on the same period last year; and the pharmaceuticals, medical and biotechnology sector, where this year's deal value of US$13.4 billion is up 26% on the US$10.6 billion worth of deals seen at the same point in 2023.

And there are reasons to be optimistic about a continued upswing in dealmaking activity over the year ahead, argues Pedersen – particularly if confidence among firms strengthens further.

"There is growing pressure on firms to make exits and to reinvest," she says. "And with interest rates now coming down at a global level, the market environment is becoming more supportive again."

PE BUYOUT VALUE BY SECTOR IN ASIA-PACIFIC (US$ MILLION), Q1-Q3 2024 VS Q1-Q3 2023



> Money needs to be deployed because funds have been raised – deals need to happen over 2025.

Dean Collins
Dechert LLP

Sustainability

Dechert contributors

Dean Collins
Singapore

Stephen Leitzell
Philadelphia

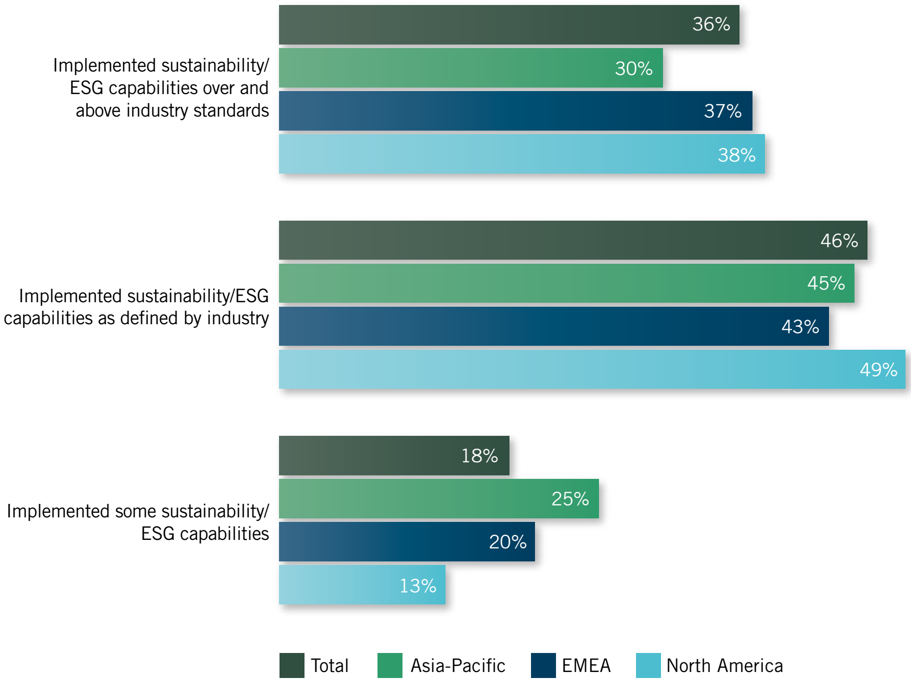
Mikhaelle Schiappacasse
London

Sustainability and ESG remain important considerations for many PE firms. As noted earlier in this report, every single PE firm taking part in this research is considering investment activity related to these themes or is at least open to the idea. The size of the opportunity is enormous: the world invested about US$1.8 trillion in clean energy in 2023 – a record amount – but this needs to climb to about US$4.5 trillion a year by the early 2030s to meet the Paris Agreement's 2050 net zero target, says the International Energy Agency. Governments and public companies clearly cannot do it alone.

And more broadly, sustainability and ESG considerations are now key factors driving decision-making at both GP and LP level.

"This is due in large part to increased LP demands for robust ESG strategies and reporting, particularly from pension funds and sovereign wealth funds, which have prompted GPs to prioritize ESG and sustainability factors," says Mikhaelle Schiappacasse, co-head of Dechert's global sustainability practice (London).

HOW WOULD YOU DESCRIBE YOUR FIRM'S PROGRESS SO FAR ON ITS SUSTAINABILITY JOURNEY? (SELECT ONE)



"In addition, regulatory developments, particularly in the EU, are pushing PE firms to enhance their ESG practices."

Indeed, a recent survey conducted by INSEAD's Global Private Equity Initiative revealed that 90% of LPs consider ESG in their investment decisions, with 77% using it as a criterion for selecting GPs.

One result is that some PE firms are now making significant investments in their capabilities in this area. Many firms are hiring staff with specialist skills or investing in technology to support monitoring and reporting. Competency is improving at both the GP level and within the portfolio management process.

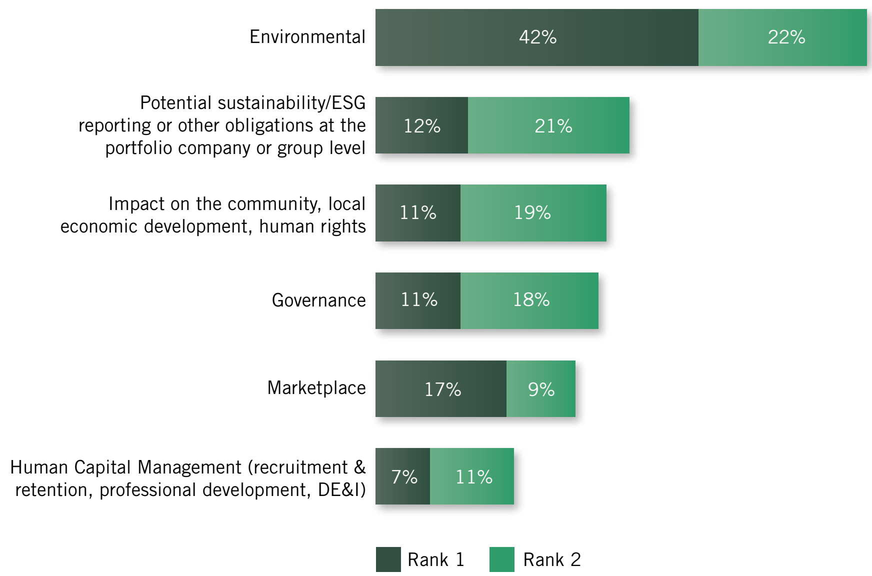
Already, more than a third of PE firms (36%) believe they have implemented sustainability and ESG capabilities that are ahead of industry standards. Just 18% think they are lagging behind by implementing only some sustainability considerations, though this figure rises to 25% among firms in the Asia-Pacific region, where ESG considerations have historically been less influential.

Nevertheless, this is an evolving picture. It is clear, for example, that many PE firms are much more focused on the "E" of ESG than on the "S" or "G". While 64% of firms in this research say that environmental considerations are critical in the portfolio investment decisions they make, only 30% and 29% point to social and governance issues, respectively.

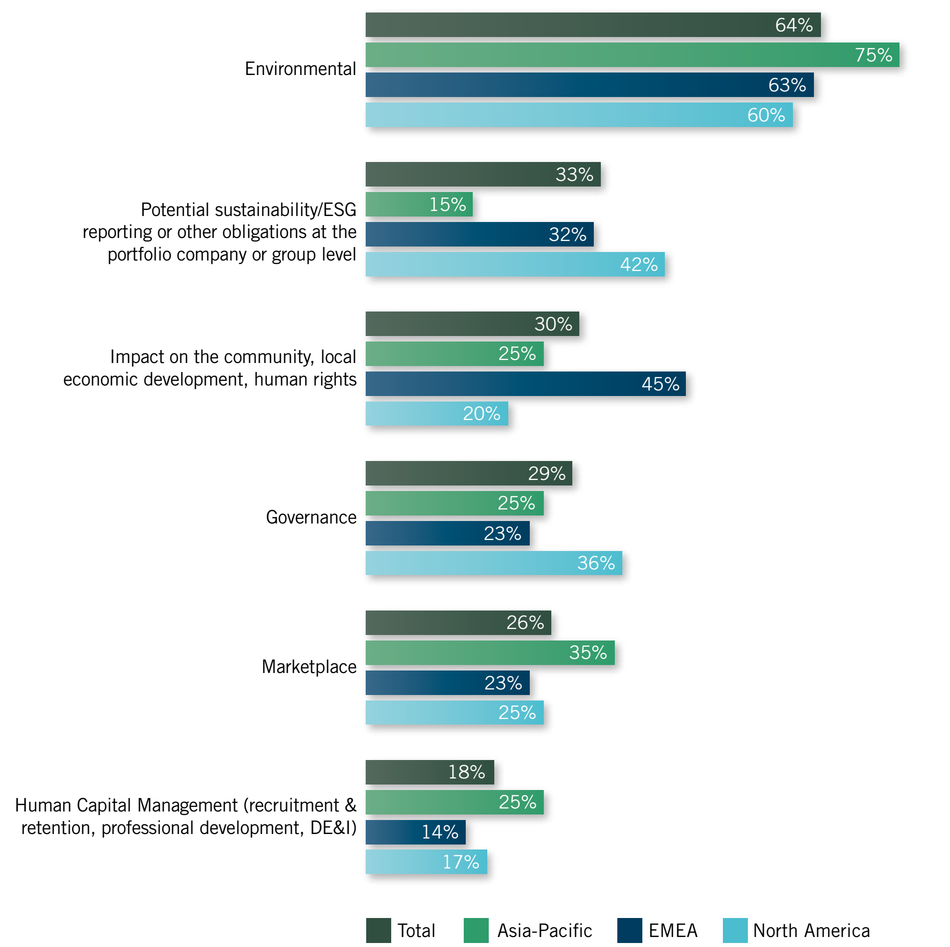
This makes sense in the context of the regulatory backdrop. The imperative to confront climate change has seen environmental regulation proliferate over the past five to ten years, particularly in Europe, but increasingly in North America and Asia too. PE firms must be aware of the opportunities and challenges their portfolio companies face in this regard.

In some cases, these considerations are existential. Certain investments look increasingly like stranded assets in a world focused on the transition to net zero. Other judgments are more nuanced. For example, firms may ask themselves: "To what extent is a portfolio company vulnerable to regulatory sanction or reputational damage in an environmental

WHAT ARE THE MOST IMPORTANT SUSTAINABILITY CONSIDERATIONS ADDRESSED AT THE GP LEVEL IN MAKING PORTFOLIO COMPANY INVESTMENT DECISIONS? (SELECT TOP TWO AND RANK 1-2, WHERE 1 IS THE MOST IMPORTANT)



WHAT ARE THE MOST IMPORTANT SUSTAINABILITY CONSIDERATIONS ADDRESSED AT THE GP LEVEL IN MAKING PORTFOLIO COMPANY INVESTMENT DECISIONS? (SELECT TOP TWO)



context?" Or: "What are the market opportunities of decarbonization?"

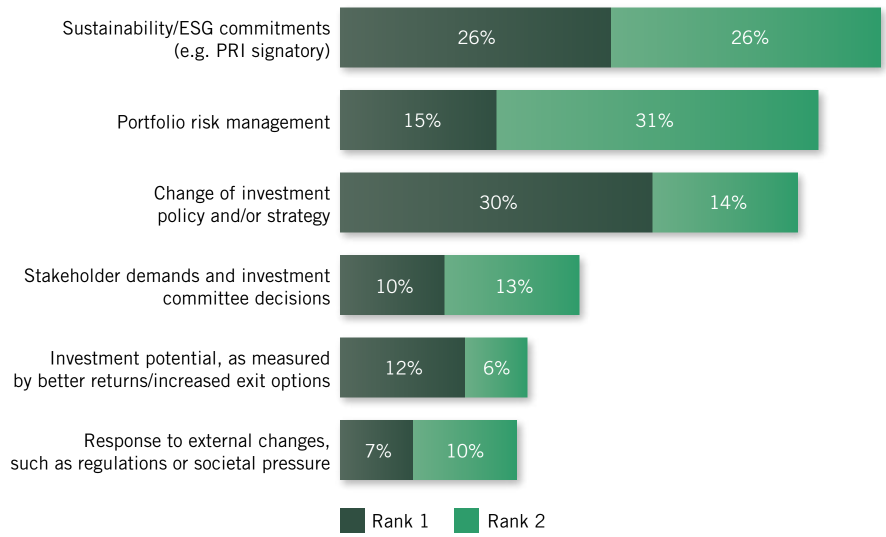
Compared to such debates, the conversation about social and governance issues is at an earlier stage in the PE ecosystem. But PE firms would be wrong to overlook these areas. The global focus on supply chain dependencies, for example, takes in arguments about issues such as community support and labor market practices; the European Union is increasingly regulating on this through directives such as the EU Supply Chain Law. Meanwhile, good governance can be crucial in creating value.

PE firms in some regions are moving more quickly on a wide variety of issues. EMEA-based firms, for example, are much more likely than their international counterparts to stress the importance of social considerations such as impact on the community and local economic development. North American firms are particularly likely to regard governance as a crucial consideration.

"At the management level, PE firms need to establish a robust compliance framework that aligns with regulatory requirements and best practices," advises Stephen Leitzell, co-head of Dechert's capital markets group and co-head of Dechert's strategic transactions product line (Philadelphia). "At the portfolio level, the PE firm should incorporate ESG criteria from the onset of due diligence to identify potential regulatory risks and necessary rectification steps."

There is also an interesting debate on the imperatives for

WHAT ARE THE MAIN DRIVERS FOR LPS WHEN MAKING SUSTAINABLE INVESTMENT DECISIONS? (SELECT TOP TWO AND RANK 1-2, WHERE 1 IS THE TOP DRIVER)



focusing on sustainability and ESG considerations. To what extent is this a defensive area of work rather than something more proactive?

The evidence from this research reveals that investors are more focused on risk than opportunity. While 46% of PE firms say that risk management is a key driver of LPs' investment decisions on sustainability, only 18% say the same of investment potential.

This picture is likely to shift over time. GPs certainly need to be aware of the additional risks that the sustainability and ESG agenda creates for portfolio companies. But there will also be significant opportunities for outsized returns from the right investments in businesses in a huge range of areas – from cleantech to renewable energy, and from green transport to environmental solutions.

In this context, several PE firms have raised large ESG-focused funds. BlackRock and Temasek, for example, pulled in US$1.4 billion for a decarbonization-focused growth fund in April this year while Eurazeo raised €700 million in an over-subscribed energy transition infrastructure fund in July.

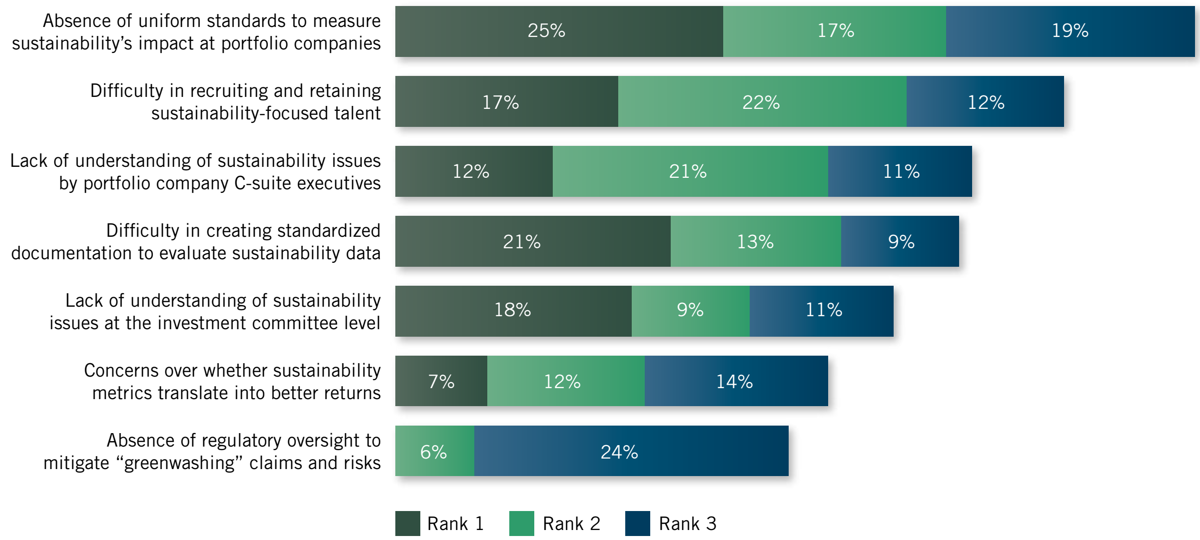
Obstacles to ESG

Despite the opportunities on offer, the PE sector is having to overcome a range of challenges as it considers whether to step up on sustainability.

At the top of the list, 61% of firms are worried about the absence of uniform standards for measuring the impact of their sustainability initiatives. In part, this reflects the lack of international consensus on ESG metrics; regulators in different jurisdictions set out different requirements and measure progress in different ways. But this is also an issue of technical competency, with new tools required to monitor impact and to report in a meaningful way.

Meanwhile, more than half of PE firms (51%) note the difficulty of recruiting and retaining people with the skills required to drive sustainability initiatives effectively. In a relatively new

WHAT ARE THE MOST SIGNIFICANT BARRIERS TO GREATER ADOPTION OF SUSTAINABILITY INITIATIVES IN YOUR FUND OR IN YOUR PORTFOLIO COMPANIES GENERALLY? (SELECT TOP THREE AND RANK 1-2-3, WHERE 1 IS THE MOST IMPORTANT)



field, where a huge number of organizations need to secure these competencies, the battle for talent has become incredibly fierce. The need for "green skills" is set to double over the next 25 years, a recent LinkedIn study found, emphasizing the difficulty of recruiting ESG professionals.

Elsewhere, there is also frustration about the difficulty of getting management at portfolio companies to engage seriously on ESG. At 44% of PE firms, respondents point to the lack of understanding of sustainability issues in the C-suite at these businesses. Sometimes, that problem is internal too, with 38% of firms conceding their own investment committees lack such understanding.

Challenges vary by region. Asia-Pacific firms are particularly likely to be anxious about a lack of uniform standards, about talent and about the difficulty of creating documentation to evaluate sustainability data. "We haven't really properly implemented ESG into our system yet," says Collins. "In developing markets with younger companies, it is hard for funds to impose strict ESG compliance requirements."

In the EMEA region, concern about greenwashing is increasing. "Europe leads on ESG regulation and reporting," points out Field. That has prompted a range of stakeholders to scrutinize claims about ESG performance much more closely, he says. In the EU, new regulation may require almost half of investment funds currently using ESG or sustainability-related labels to change names or sell assets in order to meet anti-greenwashing requirements. In addition, EU portfolio and management companies (as well as non-EU groups with significant EU operations) will also need to assess whether EU corporate sustainability reporting obligations are applicable regardless of investment focus and, if so, to factor in the cost of such compliance.

In North America, the main question is how PE firms will deal with the backlash against ESG, with politicians and others in some parts of the U.S., in particular in "red states," eager to strip such considerations out of the investment process. Bolsinger says: "There is definitely some blowback on the LP side, and GPs may opt not to take money from investors looking to restrict them from considering ESG objectives."

However, Collins says firms are working through these issues. "PE firms conduct materiality assessments to identify ESG issues most relevant to their business and stakeholders, ensuring efforts focus on areas with the greatest impact and commercial relevance.

"By employing both financial and non-financial metrics to measure performance, PE firms can align ESG goals with commercial objectives. When ESG considerations are integral to the investment thesis, firms that collect relevant data are able to substantiate how ESG contributes to long-term value creation and risk management."

Exits and other liquidity events

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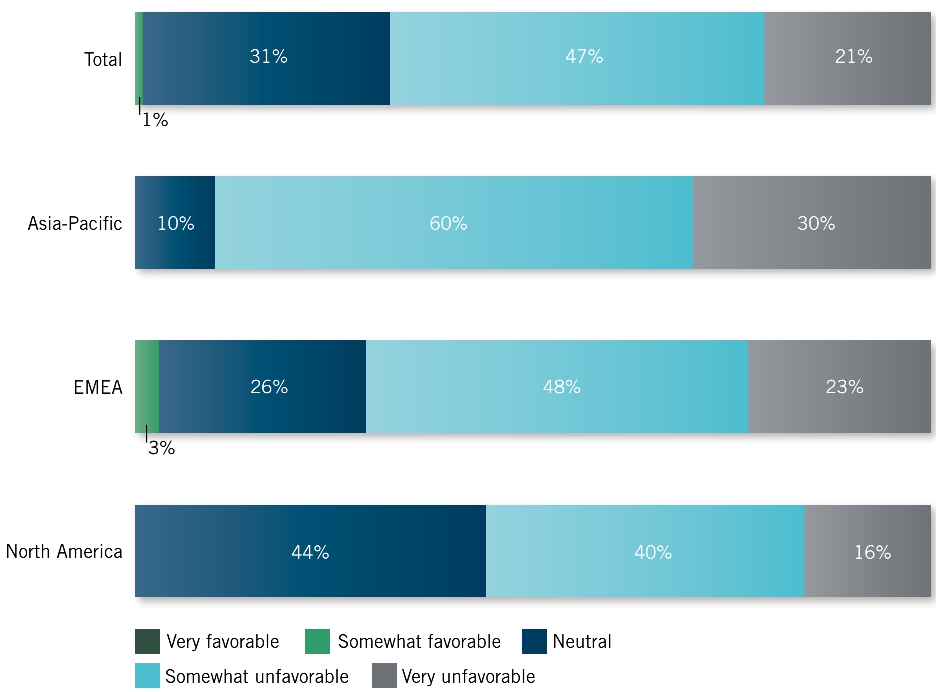
While all of 2023 and the start of 2024 proved to be tough for PE exits, there are green shoots sprouting as we head toward 2025. During the first nine months of this year, there were 1,675 exits valued at US$443 billion, up 17% and 39% respectively on the same period last year. While these figures are significantly down on those posted in 2021 and 2022, both volume and value have been rising quarter-on-quarter this year, and these increases show that confidence may slowly be returning to the exit market.

Possibly due to the slow start to exiting activity in 2024, 68% of survey respondents believe market conditions for liquidity events will be unfavorable over the next 12 months, including 21% who expect conditions to be very unfavorable. In the Asia-Pacific region, those figures rise to 90% and 30% respectively, with not a single respondent in this region expressing optimism that a recovery is on the cards. Firms in North America and the EMEA region are less downbeat – but only marginally so.

HOW FAVORABLE DO YOU THINK MARKET CONDITIONS WILL BE FOR PRIVATE EQUITY LIQUIDITY EVENTS IN THE NEXT 12 MONTHS? (SELECT ONE)

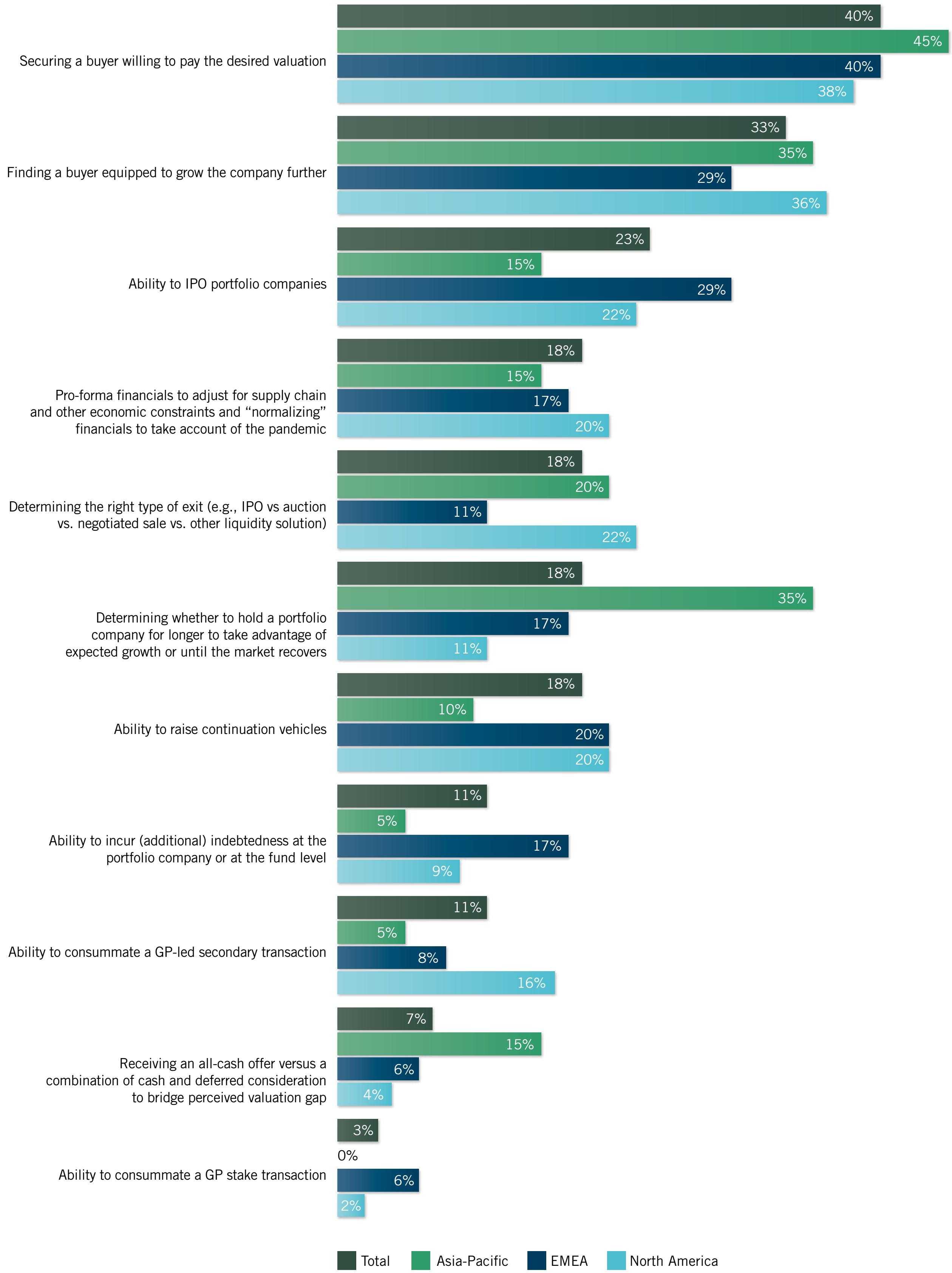


"It has certainly been hard," says Collins. "Across Asia, we have repeatedly seen funds forced to extend their lives because they still hold assets they are struggling to exit."

And, worryingly, this disruption may often have been unforeseen. In last year's research, PE firms expressed much greater optimism about their ability to secure liquidity. Only 42% of firms last year

> Across Asia, we have repeatedly seen funds forced to extend their lives because they still hold assets they are struggling to exit.
>
> 
>
> **Maria Tan Pedersen**
> Dechert LLP

WHAT ARE THE BIGGEST CHALLENGES YOU EXPECT TO FACE WHEN IT COMES TO RETURNING CAPITAL TO YOUR INVESTORS IN THE NEXT 12 MONTHS? (SELECT TOP TWO)



said they expected market conditions to be unfavorable, with 17% expecting the opposite (compared to just 1% who say the same this time around). Clearly, many of these firms were disappointed by the outturn.

> We are going to have to use the full range of tools and mitigation strategies to bridge the valuation gap.

Sabina Comis

Dechert LLP

Looking forward, despite the pick-up in activity in the latter half of the year, the difficulty for PE firms is that there appear to be multiple barriers holding firms back from a return to 2021 and early 2022 levels.

At the top of the list, the valuation gap remains intractable – buyers and sellers are simply finding it difficult to agree on price. Some 40% of PE firms describe the difficulty of finding a buyer willing to meet their valuation as one of the top two issues likely to hold exits back over the next 12 months.

Nor are other liquidity options straightforward. Almost a quarter of firms (23%) point to the difficulty of selling out of portfolio companies via IPOs; that proportion has more than doubled since last year, when only 11% of respondents shared this anxiety, even if there is now a hint of the return of IPOs in the U.S. at least. In addition, almost one in five firms (18%) cite their inability to raise continuation vehicles.

Another issue is a shortage of buyers with the credentials to take on portfolio companies. A third of PE firms (33%) worry they will struggle to find buyers who are equipped to drive growth at their portfolio businesses.

There are also distinctive regional differences in liquidity challenges. North American firms are more likely than their peers elsewhere to be worried about the difficulty of finding well-equipped buyers; they are also likely to be struggling to determine the right type of exit. Asia-Pacific firms are the most concerned about the valuation gap – and also struggle with the question of whether to hold on to portfolio companies for longer than they had originally intended; indeed, research from Bain & Company suggests portfolios in the region now carry an unprecedented number of aging investments.

In the EMEA region, meanwhile, concern about the IPO market is particularly heightened, with 29% of firms expressing doubts about their ability to list successfully. One in five firms in the region also worry about their ability to raise continuation funds. That's a real issue, says Comis, because this limits their mitigation options. "If the fund manager feels that the valuation it would get now is not the accurate one, a continuation fund is an obvious solution," she says. "It may be temporary, but it provides the fund manager with the necessary time to continue growing the asset and to then exit at the right price."

However, prospects are brighter. The slowing pace of inflation and the looser monetary policies offered by many central banks may create space for exits and liquidity events to improve over the course of 2025. Sellers' valuations may begin to look more realistic if the cost of capital falls significantly.

It's also possible that the stronger performance of many stock markets over the course of 2024 will provide a boost for IPOs. Globally, the new issues market was down during the first nine months of the year, but that was largely due to a particularly sharp decline in the Asia-Pacific region; on Western exchanges, including the U.S., activity has recovered well, providing hope that this may deliver another route to PE exits.

In that context, this year's somewhat downbeat assessment on liquidity events may prove overdone. PE firms will certainly hope that is the case. For now, the concern over exits is hindering their ability to return capital to investors; that, in turn, threatens to block the PE sector's lifecycle.

GP-led secondaries and stake divestitures

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Brian Miner
New York

The slowdown in exits and fundraisings seen over the last year is prompting PE firms to explore new routes to liquidity. In this context, GP-led secondaries and GP stakes have become more common – the trend toward both that was noted in last year's research appears to have continued over the past 12 months.

GP-led secondaries

This year, almost a fifth of PE firms (17%) expect to increase dealmaking through GP-led secondaries – and in North America, that figure rises to 22%. That will extend a trend – the volume of GP-led secondaries quadrupled over the five years to the end of 2023.

This is a good example of the agility of the sector, which is putting a wider range of tools to work as it navigates challenging market conditions. For LPs in the primary fund, there is an opportunity to cash out current LP positions or roll them into the new fund to extract additional value; GPs, meanwhile, get extra time and capital to create more value.

"Depending on the maturity of the fund, the asset class, when the next fund is likely to be raised and a number of other factors, the fund manager will pick the most appropriate tool," says Comis. "Sometimes that might mean holding the asset for longer, and in other cases it could mean organizing a GP-led exit to ensure LPs get their money back – there are a broad range of liquidity strategies available to GPs."

Importantly, however, GP-led secondaries are not purely defensive mechanisms employed by firms with few other options. That might have been the case in the past, but such arrangements are no longer automatically viewed in this light – there are plenty of positive reasons to pursue these transactions.

Indeed, PE firms are focusing on GP-led secondaries for a wide range of different use cases. Almost three-quarters (71%) see these structures as providing a means through which they may pursue more lucrative opportunities. And two-thirds (65%) are focused on the flexibility of portfolio company holding periods that these strategies can provide. By contrast, only 35% point to a lack of exit opportunities in the primary market as the main driver of their focus on GP-led secondaries.

However, Collins points out, these deals are rarely easy options. "GP-led secondaries can be very challenging – they may take 18 months to two years to complete," he says. "However, the good news is that we're seeing investors come into the secondaries market that we've not seen before – that increase in demand is very helpful."

GP-stake divestitures

On GP stakes, meanwhile, more than a third of PE firms (34%) now say they are planning a GP-stake sale in the next two years. While that is down on last year's figure of 59%, it still indicates

> "We are likely to see a further rise in GP-led secondaries in Asia."
>
> 
> **Dean Collins**
> Dechert LLP

a substantial proportion of the market is looking to bring outside investors into their management company.

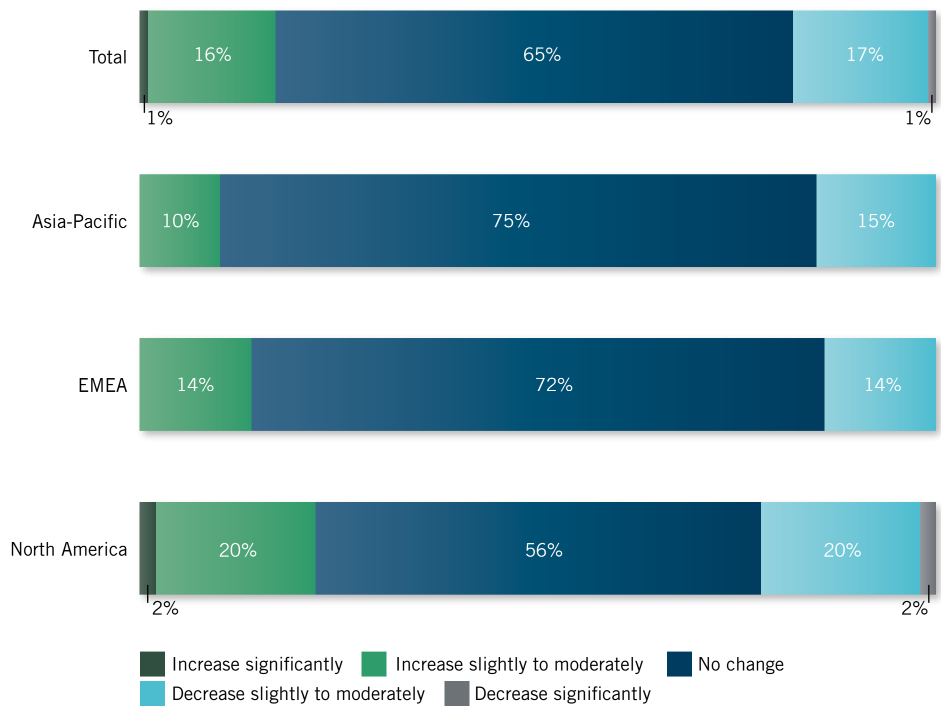
As was the case last year, PE firms in North America are particularly likely to be pursuing this option, with 44% considering a stake sale, while Asia-Pacific firms are much less likely to go down this route; only 15% of firms in the region are looking at doing so. In the EMEA region, the figure is 31%. Data from Preqin suggests that the popularity of GP-stake transactions in EMEA is beginning to catch up to North America.

"We are seeing increasing amounts of capital being raised for dedicated GP-stake strategies and it is becoming a small but significant asset class," says Kay. "This is particularly so in the U.S. where there is greater understanding of the strategic benefits, but there is an expectation that the strategy will translate to other regions."

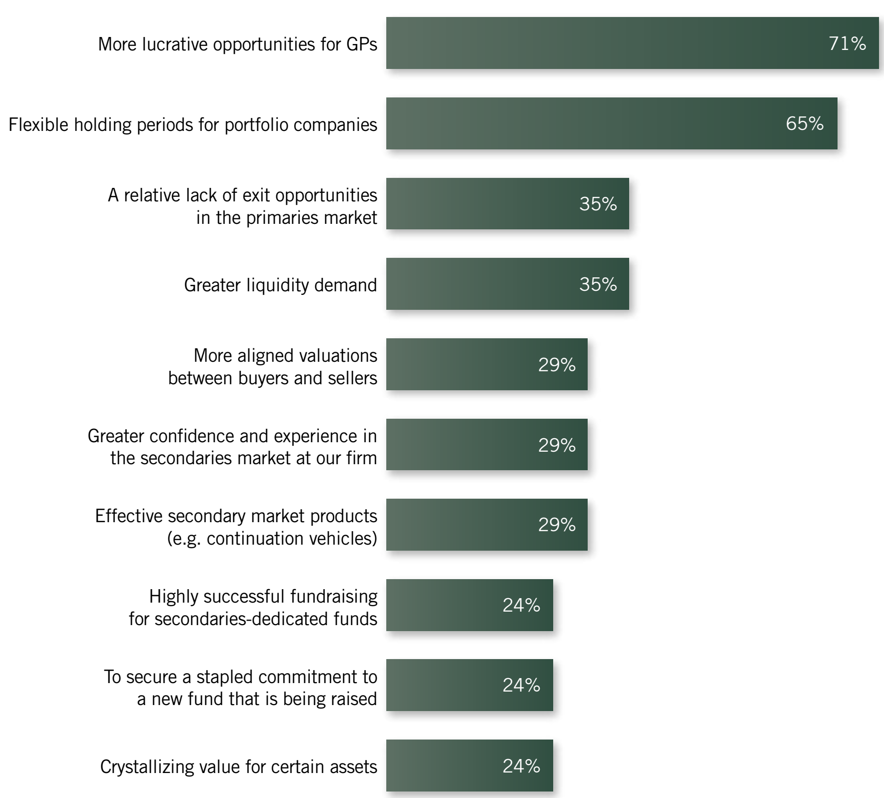
Clearly, GP stakes can work well for both sides. They offer investors a means through which they can secure more valuable access to PE managers, sharing in fee earnings, carried interest and capital gains, and potentially taking part in co-investments. As for GPs, selling a stake in the firm provides crucial liquidity – highly valuable in the current market conditions – and creates an opportunity to work more closely with investors that bring their own expertise, experience and networks.

"The increased number of investors in the space has led to better terms for managers," says Brian Miner, Dechert

IS YOUR FIRM PLANNING TO INCREASE OR DECREASE DEALMAKING USING GP-LED SECONDARIES IN THE NEXT 24 MONTHS? (SELECT ONE)



[IF ANSWERED INCREASE] WHAT IS DRIVING YOUR FIRM'S PLANNED INCREASE IN GP-LED SECONDARIES DEALMAKING? (SELECT ALL THAT APPLY)



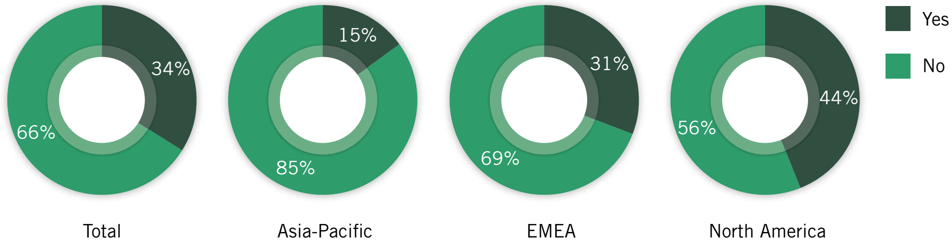
partner, corporate and securities (New York). "The type of manager receiving interest from investors has also stretched down to the middle and lower middle market, as well as to asset classes other than hedge funds and PE funds, such as real estate funds, credit funds and venture capital funds."

The other point here, says Comis, is that GP-stake divestitures can provide founders with more options. "Management company founders may be looking for liquidity as part of a generational change – because they're retiring, for example," she says. "Or it may just be a case of securing liquidity amid a delay in being able to realize carried interest."

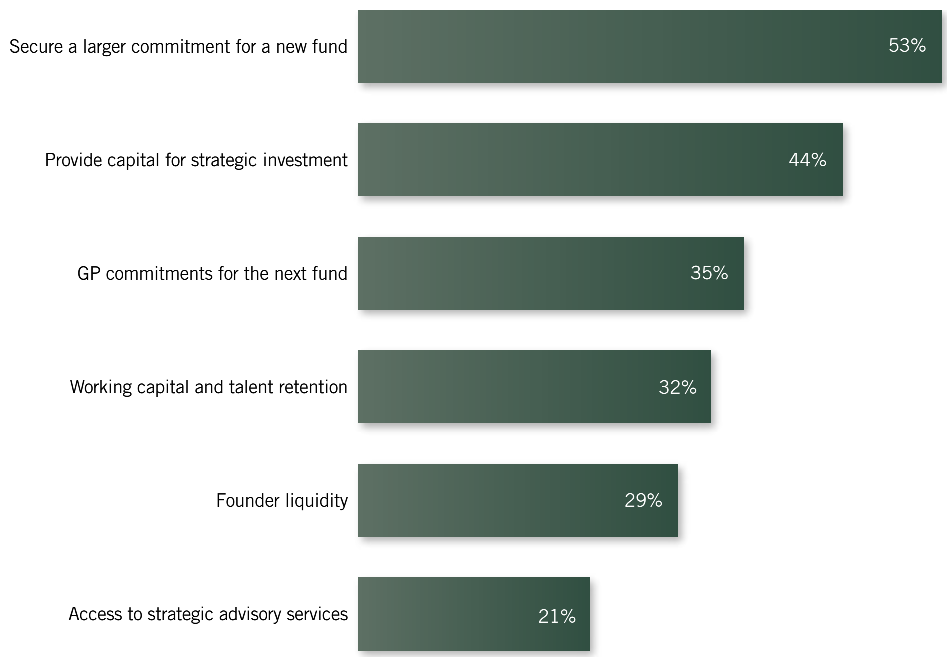
Respondents cite many of those motivations as drivers for their interest in GP stakes. More than half (53%) say they intend to use the proceeds to secure larger commitments to new funds, while 44% expect a divestiture to support their strategic investment plans.

Meanwhile, 32% stress the role of divestitures in supporting talent retention, while 29% cite the need to create founder liquidity. "We are at a point of generational change," observes Comis. "Much of the PE sector, at least outside of the U.S., dates back to the last 20 to 30 years, so we are now witnessing a generation of founders who are looking to retire."

IS YOUR FIRM PLANNING TO MAKE A GP-STAKE DIVESTITURE IN THE NEXT 24 MONTHS? (SELECT ONE)



IF "YES", WHAT WILL THE PROCEEDS GO TOWARD? (SELECT ALL THAT APPLY)



Conclusion

This year's research paints a picture of a PE sector that is in transition. There has certainly not been a return to the levels of activity seen during the boom years of 2021 and early 2022. Indeed, the slowdown in dealmaking activity that the PE sector recorded during the second half of 2023 continued into the beginning of 2024. Equally, however, there are now some signs of improvement.

The extent to which the PE sector builds on these early indications of promise will largely depend on factors beyond its control – both geopolitical and macroeconomic. GPs will be hoping that the political climate will begin to brighten, particularly following a remarkable year in which more than half the global population was eligible to vote in a general election. Meanwhile, there is cautious optimism that the global economy can bounce back more strongly, particularly as looser monetary policy makes a return.

What tempers this optimism is: international political tensions remain heightened; the economic outlook is clouded by concerns such as the difficulties facing the economy in China; and the continued march of de-globalization. Still, PE firms are doing their best to work through the challenges, employing a broad range of strategies and risk mitigations with agility and flexibility.

The key will be to accelerate the pace of the PE cycle. Interest rate reductions have the potential to support a pick-up in exits, freeing up PE firms to launch new fundraisings and, in time, to invest those proceeds in new deals. And to end on a positive note, this acceleration has begun.

> "Everyone has been saying that we need to survive until 2025 – and we have done exactly that. Falling interest rates now provide the support we need. The lower cost of credit and its availability are going to be big drivers both on liquidity for existing portfolio companies and for how you finance your deals. There is definitely now build-up for 2025."

Markus Bolsinger
Dechert LLP

As PE firms have battled through a tough 18 months, a renewed vigor has emerged in the market as we enter 2025. However, there are four key factors which could separate the outperformers from the also-rans: focusing on thriving rather than just surviving; maintaining a close watch on the private credit market; keeping up with the democratization of the market; and monitoring exposure to China.

Move on from survive, to focus on thrive

While 2024 so far may not have been a 'super-exciting' year for the sector, improving sentiment and reduced uncertainty have provided the foundations for a return to positivity. Indeed, falling interest rates now provide the support for recovery: the lower cost of credit and its availability can be significant drivers both on liquidity for existing portfolio companies and for new fundraising and dealmaking. This will also be supported by an improving outlook for exits.

Keep a close eye on private credit

The private credit sector has undoubtedly been hot, but if interest rates continue to come down, investors are likely to be increasingly selective. While there is continued interest in the private credit sector – and demand from borrowers – it's possible we will now see some reallocation of capital into other strategies, including PE.

More power to the people

The democratization of PE is going to continue. This means that what we call the private funds industry today is going to become a different type of industry, particularly as it continues to expand into different types of asset classes such as infrastructure, debt and energy. Expect further consolidation and growth of AUM. Part of this story is also about generational change: people need to retire, creating movement in the market and prompting more activity in areas such as GP-stake divestitures.

The question of China

China is still the largest economy in Asia, by a huge margin. Nevertheless, there are significant reasons why inbound investment continues to decline. That may drive more fundraising with different mandates, cutting China out of the equation, or vehicles that offer exposure only to China for those investors who want it.


Guiding your
investments to
new horizons

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