Investec

OUT OF THE ORDINARY

2022 GP Trends

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Economic update

Before we head into the main findings of this year's report, Investec's Economics Team provides some insight into the macro-economic environment.

The global economy emerged strongly from the removal of Covid-19 restrictions outside of China, the resilience of the labour market being a common noteworthy feature. However, this undoubted success had a flip side: surging energy prices, much exacerbated by Russia’s invasion of Ukraine, added an extra inflationary supply shock that looked more likely to be prolonged in such tight labour market conditions. This has left central banks across the globe scrambling to tighten monetary policy in a bid to cool demand and bring inflation back under control.

As yet, victory in the fight against inflation is elusive as labour market conditions remain tight. Fiscal support has had to be ramped up again in Europe to help deal with the energy price shock, if to varying degrees. With inflation at multi-decade highs, it is uncertain how much higher policy rates will have to be raised to bring inflation back to target. Ultimately, reversion to the ultra-low pre-Covid policy rates is no longer expected either. This has pulled longer-dated yields up too, pushing up funding costs for the government and, indirectly, companies.

Within the UK, a further complication has arisen as a result of the substantial fiscal easing plans announced by Chancellor Kwarteng in his mini-Budget. Markets were not convinced by the government’s assurances, not accompanied by an external assessment, that tax cuts would pay for themselves. On top of causing a plunge in sterling, this sent gilt yields soaring and triggered an emergency bond-buying operation by the Bank of England to prevent the collapse of certain defined-benefit pension schemes.

Through fiscal intervention, we expect recession to be averted in the UK and ameliorated in the Eurozone this winter. But sharply higher interest rates will increasingly weigh on the global economy. Recession now looks likely during H2 2023. By the end of next year, rates could be cut again in the US and also in the Eurozone; in the UK, on current fiscal policies it may take somewhat longer. All this is likely to make for a challenging backdrop for the industry. But as always at such times, dislocations will beget opportunities.

Sandra Horsfield,
Investec Economist

A quick snapshot

Welcome to the 12th annual GP Trends Report 2022, which has become established as a key bellwether for private equity (PE) industry sentiment and a signpost to the future trends shaping the asset class's direction of travel.

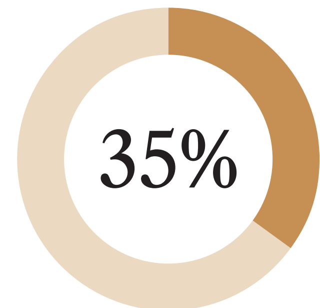
We polled over 150 GPs (general partners) for this year through a period of profound change for PE firms. After delivering unprecedented levels of deal activity and record high fundraising in 2021, the survey findings show that GPs are pausing to assess the impact of inflation, interest rate hikes and rising energy costs on investment strategies, portfolios and fundraising schedules.

But while this is undoubtedly a challenging period for PE, the industry has a proven ability to deliver value for investors through market cycles, and the survey findings show that a large number of GPs still expect to deliver better returns for clients and raise larger funds over the next 24 months.

What has been particularly encouraging about this year's survey findings has been the progress PE has made on diversity and gender equality. While there is still a way to go, the number of women and ethnic minorities working at partner level in the industry is growing, and with the survey research suggesting that firms prioritising diversity within their organisations are better equipped to attract and retain talent, the outlook for industry diversity is positive.

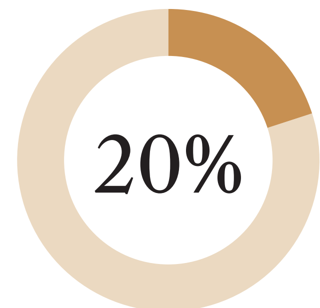
Also striking is the link this year's report finds between firms that expect to be the most successful in the fundraising market and firms following environmental, social and governance (ESG) best practice. The findings also show that most GPs believe implementing ESG at portfolio company level goes to value on exit, and that ESG is a key influencer of investor decisions when it comes to backing new funds. ESG, it seems, is swiftly evolving from an exercise driven by compliance into a key differentiator in the fundraising market and a predictor of good financial returns.

Firms that have appointed female partners during the last 12 months



For a majority of GPs, the penetration of female or partners or those from an ethnic minority is still quite low. However gender equality is a strong priority for the big 30 funds, with 43% highlighting they have appointed female partners in the last 12 months.

Firms that have appointed ethnic minority partners during the last 12 months

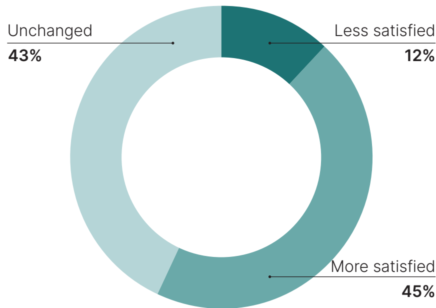


This survey finds that firms that have 25%-50% of their staff from minority backgrounds are more likely to retain their employees.

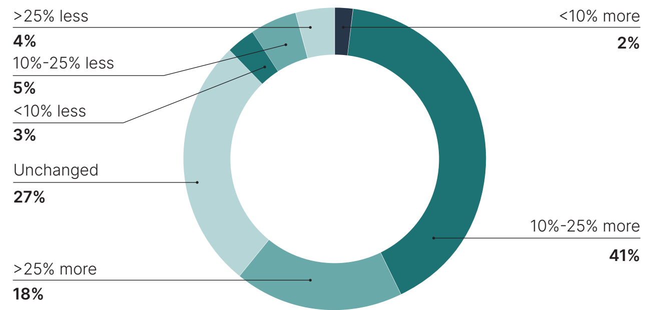
76%

ARE NOT CONSIDERING MOVING FIRMS, RETIRING OR CHANGING CAREERS

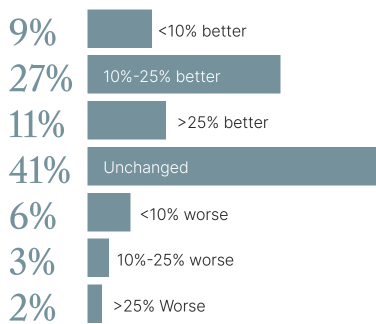
How satisfied are you with your career compared to 12 months ago?



Will your firm deploy more or less capital during the next year than the last 12 months?

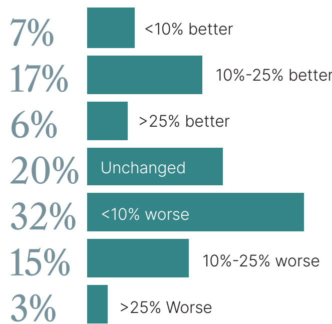


Do you expect returns at your firm over the next 24 months to be better than 2021?



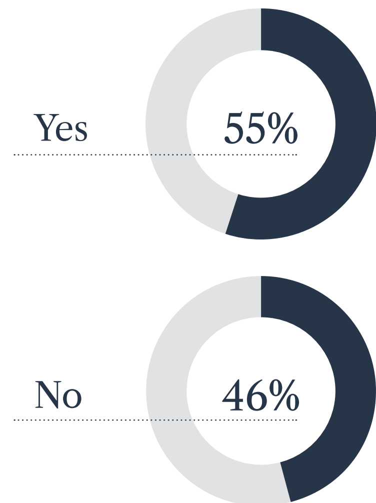
A majority expect their firms' funds over the next 2 years to be unchanged, and more than 1 in 4 expect them to be 10-25% better, which highlights a seemingly positive outlook from GPs on the industry.

How will your asset valuations move over the next 12 months?



GPs are adjusting their asset value expectations in line with financial challenges that are rocking the industry.

Do you expect to see more covenant breaches over the next 12 months?



71%

OF GPS THINK THAT RISING INFLATION AND INTEREST RATES WILL DECREASE THE AVAILABILITY OF FINANCE FOR DEALS

54%

HIGHLIGHT THAT ESG CREDENTIALS WILL POSITIVELY INFLUENCE THE LIKELIHOOD OF COMMITTING CAPITAL

Executive Summary

55%

ARE ANTICIPATING MORE COVENANT BREACHES DURING THE NEXT 12 MONTHS.

Bracing for a challenging market

The GP Trends Report findings reflect a shift in the market, with respondents preparing for more covenant breaches, lower asset valuations, tighter capital markets and lower leverage multiples.

“Across the economy businesses are facing the converging headwinds of supply chain bottlenecks, rising energy prices, tight labour markets and rising interest rates,” says Flor Kassai, Partner and Head of Buyouts at Inflexion Private Equity.

Inflation and interest rates are top of the agenda for GPs, with 71% expecting rising inflation and interest rates to decrease the availability of finance for deals and 55% are anticipating more covenant breaches during the next 12 months. More than a third (36%) of GPs are considering lowering leverage multiples to help manage cash burdens as interest rates rise.

Half of the respondents, meanwhile, expect their asset valuations to be lower over the next 12 months and 41% have seen broken deal processes during the last 12 months.

This picture stands in stark contrast to red-hot markets of 2021 when assets were flying off the shelves, liquidity was abundant and valuations full.

A resilient asset class

But while the survey findings do highlight the building headwinds facing the industry, there is nuance and context to the findings. Although GPs are pivoting onto the defensive, the industry is resilient, and responses show that GPs are still cautiously optimistic.

The majority of respondents expect to deploy more capital than in 2021. Firms still have large sums of dry powder to invest (US$3.6 trillion globally, across all private markets strategies, according to Bain & Co[1]) and may see cooling in asset valuations as an opportunity to buy quality deal targets at more attractive prices than observed a year ago.

“Nordic Capital delivered record buyout activity in 2021 so it is slightly surprising to see so many respondents expecting to deploy more capital during the next 12 months, given the uncertainty in the market, but firms have capital available and will continue to look for opportunities,” says Klas Tikkanen, Chief Operating Officer at Nordic Capital. “Deals will still be done, but my expectation is that

1. https://www.bain.com/insights/shifting-gears-private-equity-report-midyear-2022/

PE firms will be highly selective and very cautious around valuations."

Livingbridge Partner Liz Jones adds: "The macro-economic backdrop is tougher, but good investments can be made in challenging times albeit structures may require more innovation and creativity. We should also remember that disruption and innovation have always driven change and many of our investee partnerships have been with companies founded in times of dislocation and macro uncertainty."

GPs also appear to be sanguine about fundraising prospects and the outlook for returns. The majority of GPs expect their firms to raise more or at least the same amount of capital for their next funds. Some GPs are especially optimistic about the fundraising outlook. Some 46% expect the size of the next fund to exceed its predecessor by 25%-50% and a fifth of survey participants see the size of their firm's next fund exceeding its predecessor by 50%-100%.

"I do believe there is a gap opening up between funds that have a long-term track record and can demonstrate sticking to a consistent strategy and those that can't. The market is tougher, but LPs are still going to make allocations to good managers because they don't want to miss out," says Inflexion Private Equity's, Kassai.

On the returns front GPs are also upbeat although not as bullish as they were in 2021. In the 2021 GP Trends Report, two-thirds of respondents signalled that returns over the next two years would be better than in 2020. This year that proportion is down to 47%, reflecting a recognition of the potential headwinds the industry is facing in the next 24 months. A further 41%, however, expect to match returns delivered in 2021, with less than 10% of GPs worried about delivering deteriorating returns.

46%

OF GPS EXPECT NEXT FUNDS TO EXCEED PREDECESSOR BY 25%-50%

"One of the levers a PE firm will pull when a portfolio company is underperforming, and as a result pushes up against covenants because earnings have dropped, is making a change to senior management," Mark Buttler a Partner at Total Capital says. "Given the economic backdrop, and its impact on performance, the findings are in line with what I would expect."

Overall, however, GPs are showing confidence in the quality of their portfolios, with most expecting EBITDA earnings to improve.

Tough times may lie ahead, but the survey suggests that the industry is well-capitalised and well-prepared to navigate any market dislocation.

ESG to the forefront

One of the most striking findings from this year's research, however, is that links can be made between the best performing managers in the fundraising market and deal markets and the firms that are prioritising diversity, inclusion and ESG across their organisations.

"Building a diverse workplace creates a virtuous circle and has a positive impact on other areas of human resources. If candidates can see that you have an open culture and offer internal support to your people, then they will want to join and stay at your firm," Nordic Capital's Tikkanen says.

Well over half (55%) of GPs that expect their next fund to be 50%-100% larger than its predecessor are at firms that have employed a female partner in the last year. This compares to only 21% in firms that expect their next funds to be flat. Similarly, 29% of managers expecting to raise a larger fund have appointed a partner from a minority background, as opposed to a minority partner hire rate of just 17% in flat funds.

Further, 54% of respondents believe that ESG credentials will somewhat influence LPs' likelihood to commit capital to a fund and almost two-thirds (62%) say ESG has been a significant contributing factor to their decision not to invest in a company.

These findings point to the rapid evolution of ESG and diversity within private equity from a "nice to have", or exercise in box-ticking, to an increasingly fundamental differentiator in a crowded fundraising market that determines which firms are the most likely to raise funds successfully and deliver sustainable long-term returns.

> *The market is tougher, but LPs are still going to make allocations to good managers because they don't want to miss out."*
>
> **Flor Kassai, Partner and Head of Buyouts at Inflexion Private Equity**

SECTION 1

A bifurcating fundraising market

47%

EXPECT FUND RETURNS OVER THE NEXT TWO YEARS TO BE BETTER THAN IN 2021.

After reaching a high-water mark in 2021, the PE fundraising market picture has been more complex and nuanced in 2022 as investors have paused for breath to assess their exposures and whether falling stock markets will bring the denominator effect into play, requiring LPs to trim private equity portfolios.

At the same time as LPs have adopted a more cautious approach to making new private equity commitments, a number of blue-chip private equity brands have come to market within months of each with substantially larger funds. Simply re-upping commitments to these top performers has absorbed the bulk of LP budgets for 2022, leaving little over for other firms hoping to raise new vehicles.

This year's survey findings reflect this transition in the market and point to a private equity landscape that looks like it will become increasingly bifurcated over the next 12- 24 months.

"Over the next ten years there is still significant room for the PE industry to grow, but investors will become more and more selective, with managers in the top two quartiles for performance raising a disproportionate amount of capital," Nordic Capital's Tikkanen says.

A fifth of GPs expects the size of their firm's next fund to exceed its predecessor by between 50%-100% and 46% anticipate their next fund to be between 25%-50% bigger

than their current vehicle. This leaves a third of managers who are preparing for flat fundraises next time they go to market.

A similar picture emerges when it comes to returns expectations. Around half of firms (47%) expect their returns over the next two years to beat their 2021 returns, but more than half anticipate flat or declining performance.

These splits in the market could have long-term implications for the shape of the industry. Some firms will be able to continue securing and deploying capital and attracting talent, but others may struggle as investors take a more selective approach to backing new funds and favour established names with long-term track records.

Almost two-thirds (63%) of respondents in the larger funds category also anticipate superior returns over the next 24 months to be better in 2021, with only 37% of the flat funds group as optimistic.

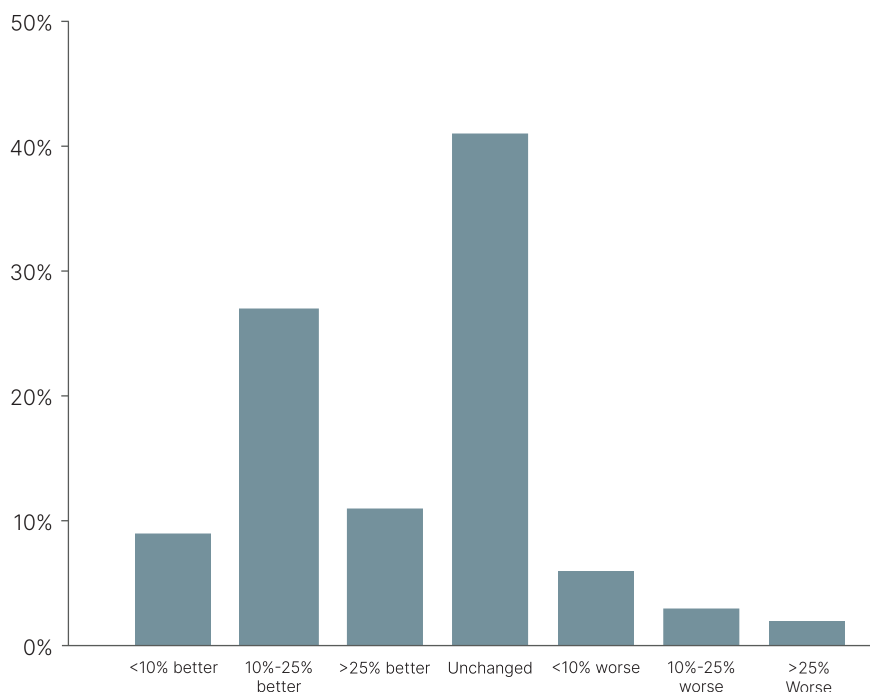
Three-quarters (73%) of GPs expecting larger fundraises also expect to deploy more capital in the next year, versus just 33% of GPs with flat funds.

Macro-economic headwinds have not scared LPs off private equity by any means, and managers with quality track records are likely to continue raising oversubscribed funds that are larger than their predecessors. The quality bar, however, is sitting higher than ever and in challenging market some GPs will find it increasingly challenging to raise and invest funds and build teams.

"Over the next ten years there is still significant room for the PE industry to grow, but investors will be become more and more selective, with managers in the top two quartiles for performance raising a disproportionate amount of capital."

Klas Tikkanen, Chief Operating Officer at Nordic Capital

Do you expect returns at your firm over the next 24 months to be better than 2021?



SECTION 2

Doubling down on asset quality

1/2

OF GPS EXPECT NEXT FUNDS TO EXCEED PREDECESSOR BY 25%-50%

41%

HAVE SEEN BROKEN DEALS PROCESSES DURING THE LAST 12 MONTHS

In the same way as reading PE fundraising trends has become trickier through the course of 2022, so has anticipating the drivers of PE dealmaking in a volatile and uncertain market.

On the one hand, GPs have vast amounts of capital to deploy – Bain & Co puts global dry powder levels across all private markets strategies at an all-time high of US$3.6 trillion – and the survey shows that they are determined to invest it, with 61% of respondents expecting their firms to deploy more capital during the next year than over the last 12 months.

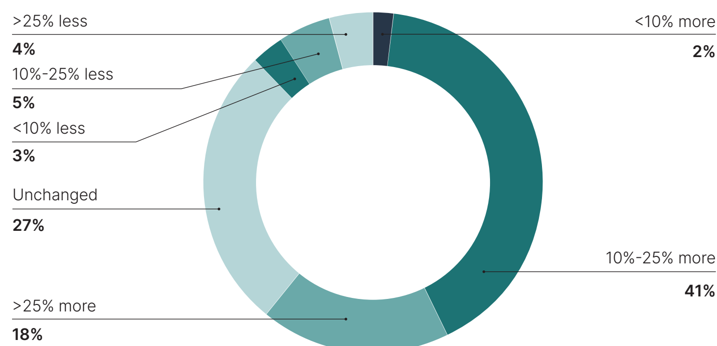
"The private equity industry knows that it has to stay active throughout the economic cycle and that investors want to see reasonably consistent levels of deployment across all vintages," says Livingbridge's Jones.

At the same time, however, the survey does show a recognition within the PE community that the bull deal market observed in 2021 has softened and that closing deals could take longer and prove more challenging in the coming months.

Half of GPs expect asset valuations to fall, which could put the brakes on deal activity as vendors, who would have fetched full prices for assets in 2021, hold off bringing deals to market until the pricing rebounds.

"All the levers that drive valuations are under pressure. Market sentiment and benchmark stock market valuations have come down; debt costs are rising and debt availability is tightening so the prices PE is able to pay should be lower; and dealmakers will be very cautious about business plans and earnings forecasts," Graphite Capital Managing Partner Markus Golser says.

Will your firm deploy more or less capital during the next year than the last 12 months?



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Markus Golser, Managing Partner at Graphite Capital

Shifts in pricing expectations between vendors and buyers could also explain the high levels of broken deals reported in the survey, with 41% of respondents observing broken deal processes in the last 12 months.

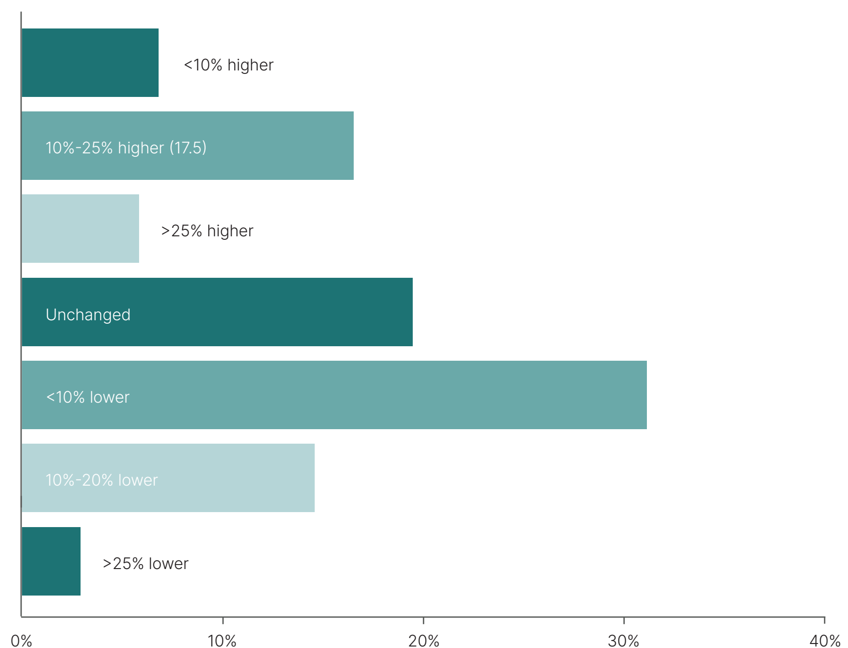
The survey also suggests that there is a pivot in PE towards more defensive sectors in a volatile economy. The resilient and stable Healthcare (77%) and business services (65%) ranked as the most attractive sectors for GPs in 2022.

"Many PE firms across the market will be telling advisers that anything with a consumer angle, and particularly big-ticket items for the home, is going to be off the table for now. Many GPs will be narrowing down their focus to assets in the most resilient sectors," Total Capital's Buttler says.

Surprisingly, only 25% of respondents ranked TMT as an attractive investment sector, down on the 47% of GPs who favoured tech deals in 2021. The low ranking for technology assets may be overdone, given how pervasive and crucial technology and digital capability have become across all industry verticals, but the findings may reflect corrections to valuations of private and public technology companies through the course of 2022. TMT deals, however, remain a key driver of PE deal activity, with White & Case and Mergermarket figures showing that TMT has delivered significantly more M&A deal value globally than any other sector[2].

2. https://whcs.law/3LUShzS

How will your asset valuations move over the next 12 months?



"We are seeing a bifurcation in the market between portfolio companies and deals exposed to consumer and industrials, where cost of living and energy costs are a big challenge, and businesses in non-cyclical industries."

Flor Kassai, Partner and Head of Buyouts at Inflexion Private Equity

Against a challenging backdrop, the deal market appears to be bifurcating as PE firms cluster around a select group of high-quality defensive deal targets providing non-discretionary services and products. The fact that firms have to keep investing their capital war chests will see these elite assets continue to secure high valuations and draw substantial interest in competitive auctions.

"We are seeing a bifurcation in the market between portfolio companies and deals exposed to consumer and industrials, where cost of living and energy costs are a big challenge, and businesses in non-cyclical industries," Inflexion Private Equity's Kassai says. "For businesses in the second group pricing has barely budged from what we saw last year, and earnings continue to grow. If you look at sectors exposed to inflation and consumer spending, however, there are more broken deal processes and weaker portfolio company performance."

Total Capital's Buttler adds: "There is still money that has to be invested, and if a good asset comes to market PE firms will be interested. Sector will come into it and the quality bar will be higher, but we will see deals done."

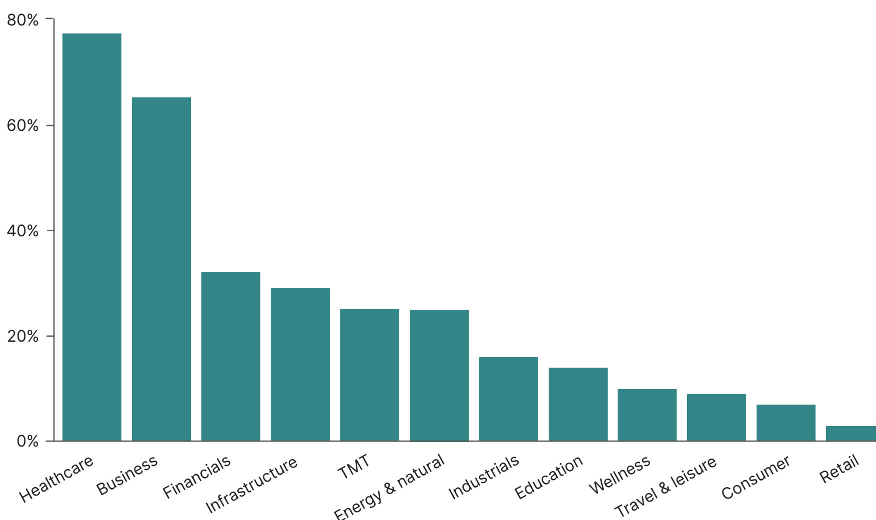
GPs, however, do appear to be more cautious and pickier about deals, and will walk away if any wrinkles appear in due diligence and will also take more time to assess target quality. Only the very best assets will pass muster.

"The number of broken deals is trending higher, and I wouldn't have been surprised to see an even higher level of bust processes. GPs are becoming a lot pickier in their due diligence and are much more risk averse when wrinkles emerge," Richard Pindar, CEO and Co-founder of Literacy Capital, says.

55%

EXPECT TO SEE MORE COVENANT BREACHES DURING THE NEXT 12 MONTHS

Which of the following sectors do you think are likely to be most attractive for investment over the next 12 months?



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>
> **Richard Pindar, CEO and Co-founder of Literacy Capital**

SECTION 3

Portfolio preservation

54%

EXPECT EBITDA GROWTH ACROSS PORTFOLIO OF BETWEEN 10%-25%

This is a challenging time for private equity-backed portfolio companies, which are having to cope with myriad headwinds ranging from staff and supply chain bottlenecks, wage and materials inflation, rising energy costs and increasing interest rates.

Despite the multitude of challenges, however, the survey findings show that most GPs are relatively confident in the quality of their portfolios and their ability to see out this testing period. Indeed, more than half of (54%) expect to see EBITDA growth across their portfolios of between 10%-25%.

This confidence in portfolios, however, should not be mistaken for complacency. GPs are under no illusions about the challenges ahead, with 55% expecting to see more covenant breaches during the next 12 months. Almost a fifth (17%) expect to be handling covenant breaches across more than 25% of their portfolio.

"There are a substantial number of PE portfolio companies with traditional covenant structures in place. Combine the impact of rising interest rates, higher input costs, margin squeeze and the real risk of lower earnings growth and it is inevitable too that covenants will be broken," Nordic Capital's Tikkanen says.

GPs are also preparing to adjust to tighter debt markets and expect to see lower leverage multiples on deals and lower debt availability. 71% of GPs think that rising inflation and interest rates will decrease the availability of finance for deals and more than a third (36%) consider lower leverage to help manage the cash interest cost burden as rates rise.

Tightening debt markets are filtering into deal structures and asset valuations.

"Expectations of lower valuations are tied into higher debt costs and tighter credit markets. Debt availability and cost determine what prices buyers can pay, so I would expect pricing to come off the multiples from a year ago," Literacy Capital's Pindar says.

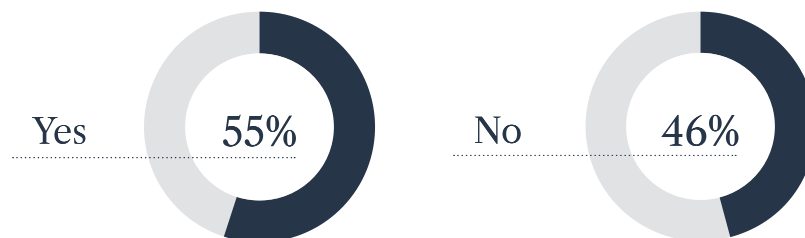
These positions on debt financing stand in stark contrast to where the market stood a year ago, when debt was commoditised and abundant, and GPs could negotiate with lenders in a competitive market to provide large sums of debt on loose terms and at low prices. As credit markets recalibrate, long-term relationships will come to the fore as PE firms look to partner with trusted lenders through this period of volatility.

"The market is still readjusting to the changing macro backdrop, but as debt supply tightens, relationships and track record will be increasingly critical. As a GP you may end up with a small pack of lenders, but as long as those lenders are reliable and deliverable, deals should be doable," Livingbridge's Jones says.

In response to the pressures companies are under, GPs are taking a hands-on approach to steer portfolio companies through this volatile period and will not hesitate to take tough decisions if deemed to be in the best interests of a business.

On the financing side, GPs are already adjusting. Two-thirds expect to apply lower debt multiples on new acquisitions, highlighting how the market is taking a more conservative position on financing. Firms are also exploring new options to secure capital in a tighter market, with more than a fifth (22%) considering using NAV debt facilities at fund level.

Do you expect to see more covenant breaches over the next 12 months?



"PE firms are aware of the challenges and are pulling all the levers they can to protect their portfolios. Hedging interest rates, scenario planning for what happens when interest rates or energy prices reach certain thresholds and looking for opportunities to keep costs down are all options," Kassai says. "You will also see firms pay out cost of living bonuses to help support and retain staff, and look for opportunities to pass costs on early before input, production and labour costs rise."

More than half of respondents (54%), meanwhile, expect to replace senior management at a portfolio company during the next 12 months, reflecting a determination to ensure that portfolio companies have the experience and leadership to see out any downturn.

"The levels of management change are much higher than normal, but it shows firms recognising that the leadership and skills required to grow the top line in a buoyant market are very different to what is needed to stabilise a business and see out a difficult period," Kassai says.

According to Literacy Capital's Pindar adds that firms are also assessing management more closely in new deal situations, which could be a factor in the rising number of broken deal processes.

"Many private equity firms do not like to change management and instead back MBOs with complete management teams, however given current circumstances I wouldn't have been surprised to see an even higher rate of change," Pindar says. "There could also be a link with increased focus on the strength of management teams pre-deal and broken deals. PE firms are not just looking for businesses that they like, but teams that they like. If there are teams they are not comfortable with, they will pull out of processes."

Total Capital's Buttler adds, however, that it is important to put the findings on management change in context and acknowledge that private equity firms do change management teams across all phases of the economic cycle.

"It is broadly the case that PE firms do not like to change management, but it is important to remember that in our part of the market management teams will very often be incomplete when private equity firms first invest, so change is always to be expected." Buttler says. "Sometimes an existing management team hits a glass ceiling in terms of their skillset and needs to be supplemented or changed."

SECTION 4

Diversity and ESG move beyond compliance

55%

OF PE MANAGERS THAT EXPECT THEIR NEXT FUND TO BE 50%-100% LARGER THAN ITS PREDECESSOR HAVE EMPLOYED A FEMALE PARTNER IN THE LAST YEAR VS 21% IN FIRMS THAT EXPECT THEIR NEXT FUNDS TO BE FLAT.

29%

OF MANAGERS EXPECTING TO RAISE A LARGER FUND HAVE APPOINTED A PARTNER FROM A MINORITY BACKGROUND VS 17% IN FLAT FUNDS.

This year's survey findings have revealed interesting links between good fundraising performance and focusing on diversity and ESG.

More diverse firms are much more confident about future fundraising than firms who have hired fewer female and ethnic minority partners.

The survey further indicates that diversity within an organisation is also becoming a characteristic of firms with stable teams and good staff retention.

Firms that have 25%-50% of their staff from minority backgrounds are more likely to retain their employees, with only 20% considering leaving. Job satisfaction is also much higher in a firm where GPs highlight that 25%-50% of the carry pot is allocated to dealmakers from a minority background.

There is still a long way to go on diversity in the industry – only a fifth of firms have appointed a partner from an ethnic minority background in the last 12 months and only 35% have appointed a female partner in the last 12 months. These figures nevertheless reflect progress for the asset class compared to prior years.

"The private equity industry is not as diverse as other industries and still has a way to go, but since I started my career there have been huge strides made to address that. LPs have wanted to see more diverse managers GPs have responded and pushed that through their organisations," Inflexion's Kassai says. "There is no single solution to making the industry more diverse, and what we want to avoid is a situation where you are promoting people above their capability or experience level. The industry has to look at all the things it can do in the round, whether that be good maternity packages and providing mentoring and coaching support to demanding that recruitment agencies find more female and minority candidates with the right experience."

Deepening the talent pool of female and minority candidates will be essential if the industry is to continue making progress on diversity and inclusion.

Finding talent is still difficult, although there is optimism that a broader range of candidates will start entering the industry on the back of diversity initiatives across the wider financial services market.

"The large professional services firms and banks have all made a concerted effort to recruit and train staff with more diverse backgrounds. As those candidates qualify and build experience I'd hope the candidate pool will deepen," Literacy Capital's Pindar says.

Drawing from this growing talent pool will be essential to avoid staff churn and encourage firms to cast the net wider when recruiting.

"The work of organisations like Level 20 has done a huge amount to improve diversity across the industry but finding and retaining candidates remains very

challenging," Graphite Capital's Golser says. "There is a premium on diverse talent, and what PE must avoid is a situation where firms are thinking twice about hiring a female or ethnic minority candidate because they are worried that in six months that person is going to be headhunted by someone else."

When it comes to sound ESG practice, it appears that the most successful funds and firms are also more likely to be the organisations leading on ESG implementation internally and on deal selection processes and capital structures.

With respect to fundraising, 54% of respondents believe that ESG credentials will somewhat influence LP likelihood to commit capital to a fund; and when it comes to deals, GPs expect portfolio companies that have good ESG processes in place to price at premiums of 10% or more when exited. GPs are also increasingly wary of the value destructive potential of ESG risk, with 62% saying ESG has been a significant contributing factor to their decision not to invest in a company.

"The weighting of ESG in LP allocation decisions is increasing steadily every year. PE Managers in Europe, and the Nordics in particular, were early adopters of ESG processes within their firms and have benefitted from the growing focus on sustainability by investors globally," Nordic Capital's Tikkanen says.

Literacy Capital's Pindar believes his firm, which is a listed investment trust that donates 0.9% of net assets in cash to literacy charities, has gained traction with investors because of its charitable contributions.

It is interesting to note that of the more than 350 investment trusts, we are the only one making this kind of donation. Of all of the trusts focused on private equity, we are the only one with a share price that trades at a premium to NAV. We are delivering the financial returns, but I do think the charity commitment is one factor that helps to put us on investors' radars too," Pindar says.

On debt structures, firms expecting to raise larger new funds are also leading when it comes to the uptake of and monitoring of ESG-linked debt facilities. These ESG-linked debt facilities have risen to prominence following the COVID lockdown period and implement margin ratchet mechanisms, which can either increase or decrease the interest rate costs on borrowings depending on a GP's compliance with pre-agreed ESG performance indicators such as carbon emission reduction or diversity targets.

This year's survey shows that 48% of firms have a board-level review in place to report KPIs for ESG-linked debt facilities, with close to a third (30%) now bringing in external auditors to review compliance with ESG-linked debt KPIs. Again, a bifurcation emerges here between firms that expect to raise larger funds and firms anticipating flat future fundraisings.

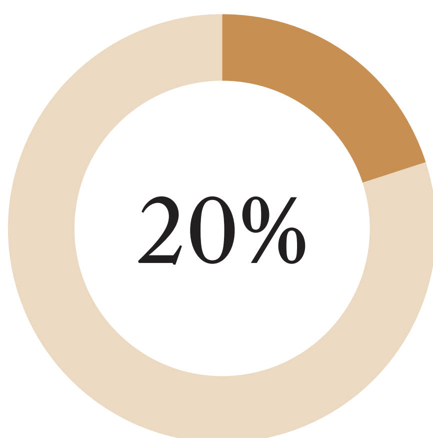
Some 53% of firms expecting to grow funds report on ESG debt KPIs at board level, versus 29% for flat funds. Strikingly, half of flat funds don't track ESG debt KPIs at any level, as opposed to almost a third (32%) of managers preparing to raise larger funds.

Overall, the findings suggest that ESG and diversity are evolving beyond exercises in compliance and public affairs into key predictors of effective fundraising and good returns, signalling a step change in how investors and firms are approaching ESG and diversity in their day-to-day business.

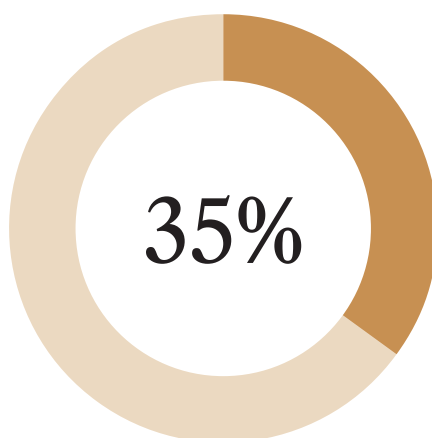
54%

OF RESPONDENTS BELIEVE THAT ESG CREDENTIALS WILL SOMEWHAT INFLUENCE LP LIKELIHOOD TO COMMIT CAPITAL TO A FUND

Firms that have appointed ethnic minority partners during the last 12 months



Firms that have appointed female partners during the last 12 months



Conclusion

We hope that you have found our annual report a valuable read and that the views and experiences we have collated from the PE community will provide insight and some answers to the questions the industry is grappling with at a time of great change for PE and the wider economy.

This year's survey reflects an industry at an inflection point. After a frenetic period of deal and fundraising activity, characterised by abundant liquidity and a bullish outlook; rising inflation and interest rates, geopolitical conflict and soaring energy costs have seen the industry recalibrate expectations and prepare to navigate a challenging period ahead.

Despite the headwinds PE is encountering, GPs remain optimistic about the long-term outlook for the asset class and are determined to protect portfolios and continue delivering value and growth for investors, management teams and the businesses they back. PE is under no illusions about the difficulties that lie ahead, but the survey findings show a community that still plans to grow its assets under management, continue investing and drive earnings growth across its portfolio.

What is even more encouraging is that PE sees sustainability, inclusion, diversity, and responsible stewardship as core to delivering returns to investors.

This year's survey shows that firms with diverse teams and credible ESG track records are already standing out from the crowd and the most likely PE shops to raise the biggest funds, close the most attractive deals and recruit the best talent.

As you look ahead to 2023, we are here to support you across all aspects of your business and make the most of the opportunities and challenges the industry will navigate in the coming months.

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