



PRIVATE EQUITY OUTLOOK & REVIEW

2024 INVESTMENT OFFSITE

MAY 2024

NEPC Research



TOPICS

- Private Equity Outlook
- Year-in-Review & Outlook
- Key Theme: Buyout Value Investing



NEPC PRIVATE EQUITY KEY THEMES

FREE CASHFLOW MATTERS

Theme: Strategies are shifting from growth at any cost to a balanced emphasis on growth with a keen focus on cash flow management

Risk: Leveraging is becoming costlier, necessitating companies to uphold sufficient cash reserves to meet interest expenses. Return expectations are anticipated to decrease.

Opportunity: Prioritizing managers with the skill set to generate returns without relying heavily on financial engineering

COMPETITIVE LANDSCAPE CONSOLIDATION

Theme: A shift toward quality, evident in a decline in the number of funds being raised from recent historic highs

Risk: Anticipated challenges for some managers in raising capital, especially high fundraising risk for newer entrants

Opportunity: Accessing high-quality managers as Limited Partners reduce their commitments. Reduced competition in the market is expected to drive lower valuations.

VALUATIONS ARE COMING BACK TO EARTH

Theme: Foresee continued downward pressure on both buyout and venture pricing throughout 2024

Risk: Anticipate devaluations for existing investments

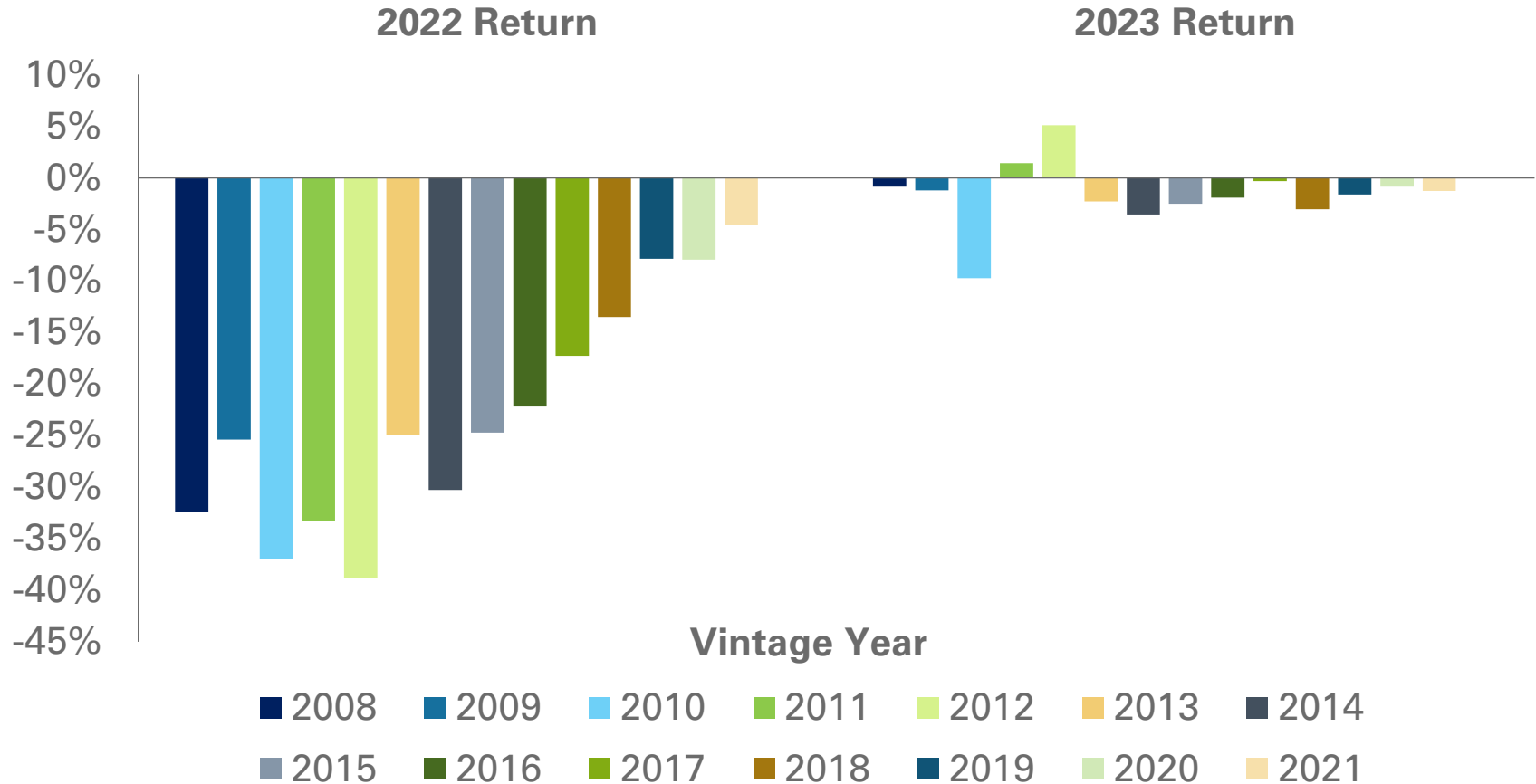
Opportunity: General Partners have been scaling back their pace of deployment for the past 12 to 18 months. As companies deplete their cash reserves, management teams are likely to recognize that current valuations represent a significant discount compared to the previous 24 months.

YEAR-IN-REVIEW & OUTLOOK



VENTURE TOOK SOME PAIN IN 2022

GIVEN LAST ROUND PRICING METHODOLOGY, THERE MAY BE MORE TO COME

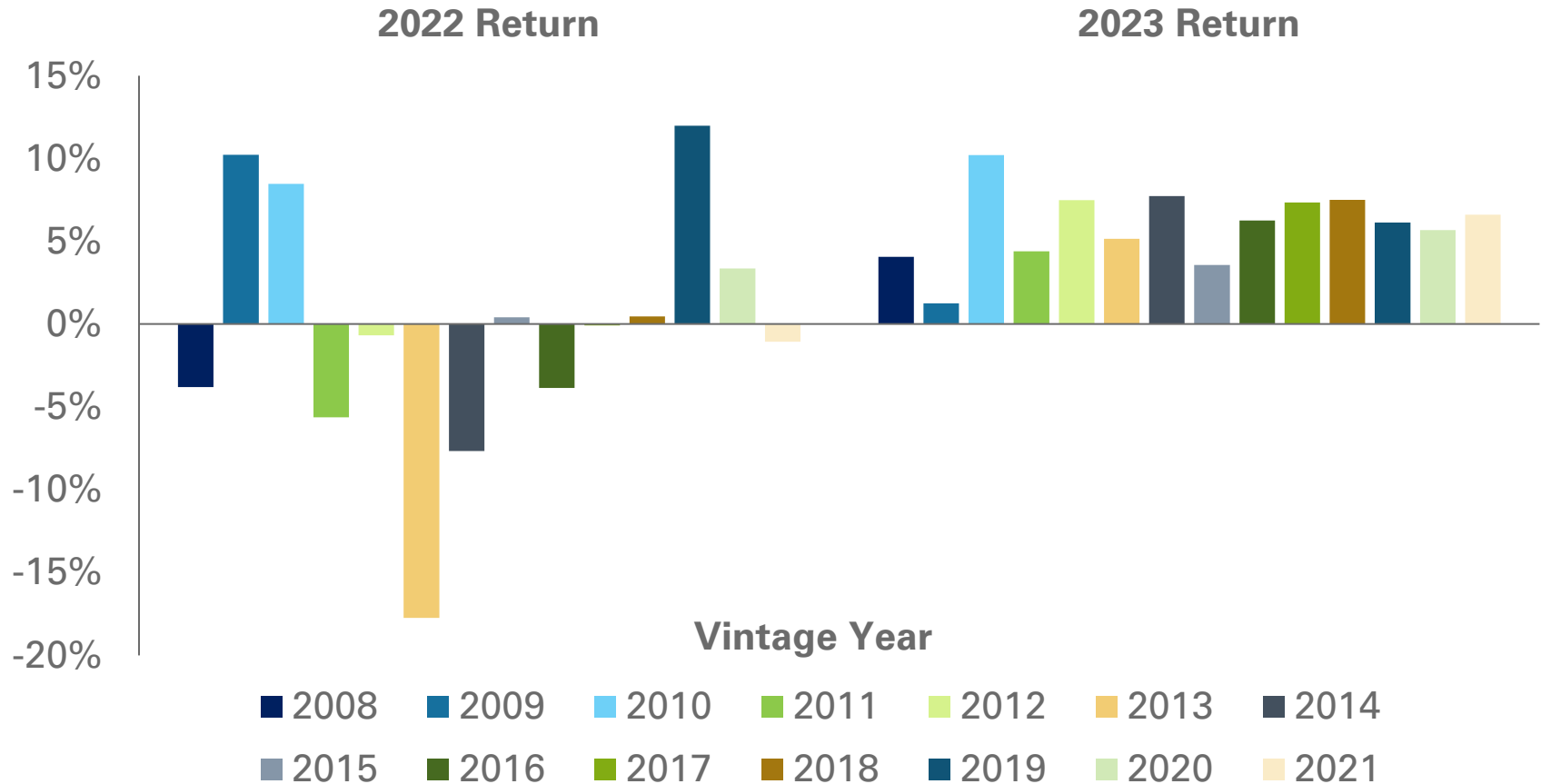


Source: C|A as of 06/30/2023. Data is net of fees.

BUYOUT RETURNS HAVE BEEN LESS HOMOGENOUS ACROSS VINTAGES

Exhibit B: Page 6

VALUATIONS TEND TO BE BASED ON COMPANY FUNDAMENTALS

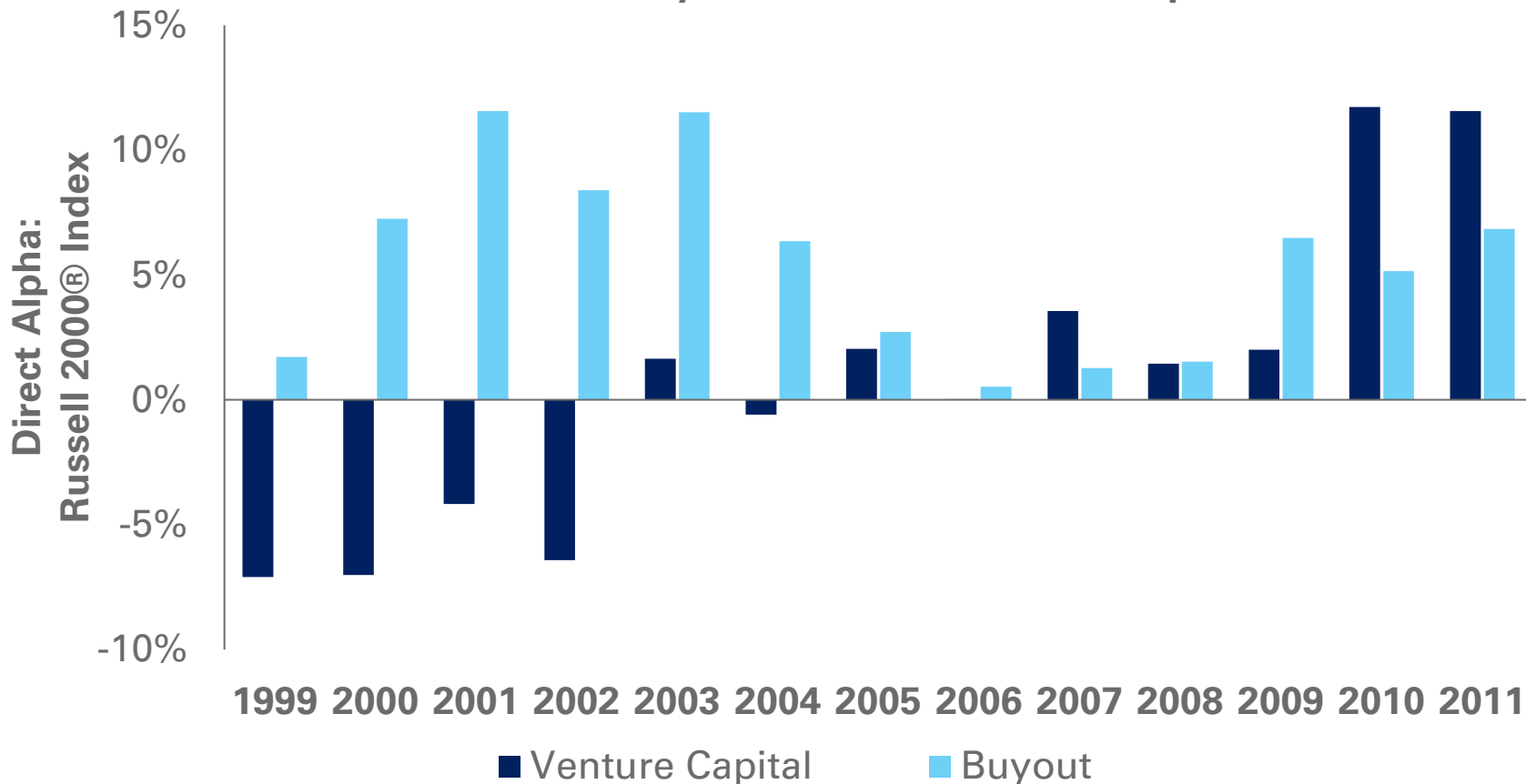


Source: C/A as of 06/30/2023. Data is net of fees.

PUBLIC MARKET EQUIVALENT

STRONG RISK ADJUSTED RETURNS POST-RECESSION PERIODS

North America Buyout and Venture Direct Alpha Returns

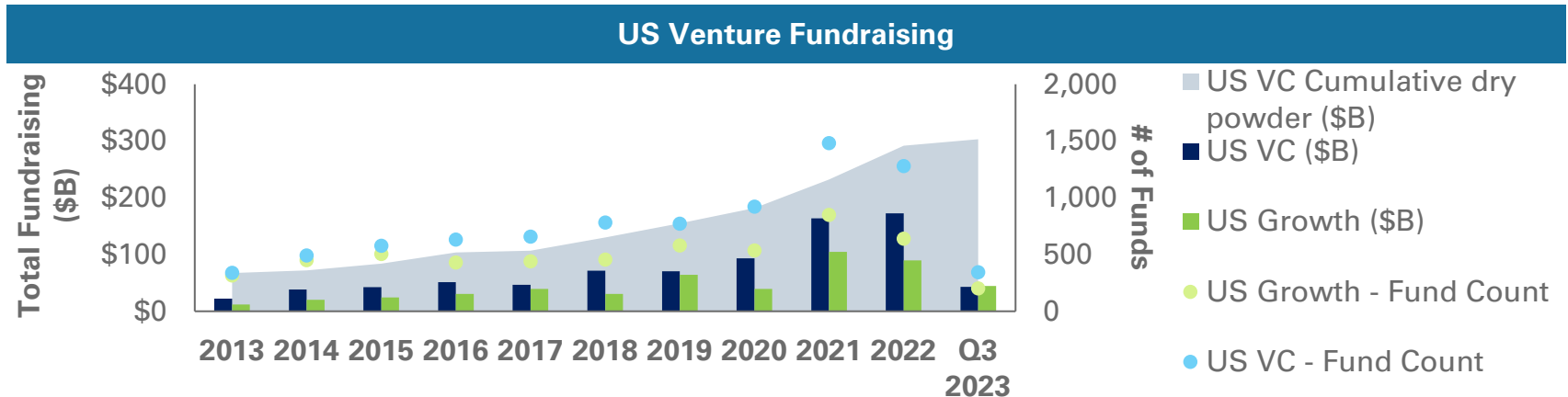
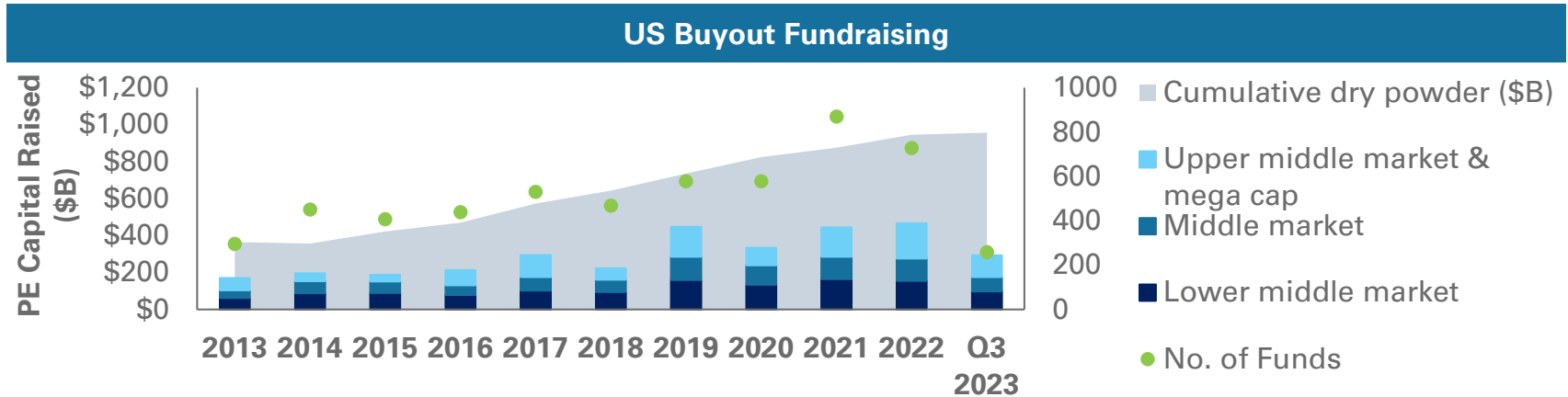


Source: Thomson One/C|A as of 06/30/2023. Data is net of fees. PE Out/Underperformance is shown based on a PME using the pooled cash flows of all funds. 1st Quartile outperformance will be meaningfully higher. PME method is Direct Alpha and benchmark is Russell 2000.



PRIVATE EQUITY FUNDRAISING

FUNDRAISING DOWN FROM ITS PEAK IN 2021

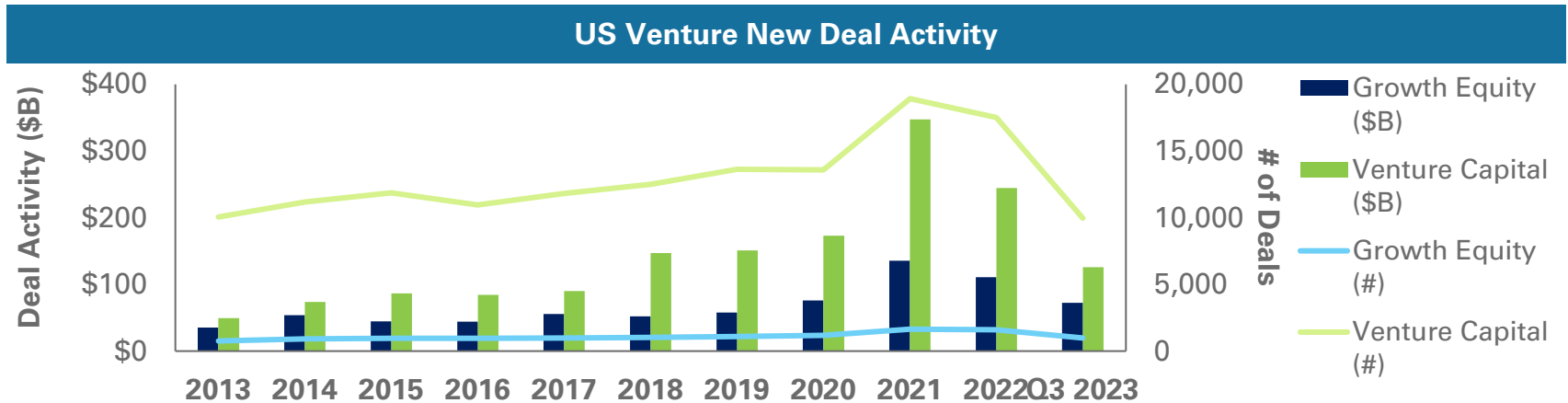
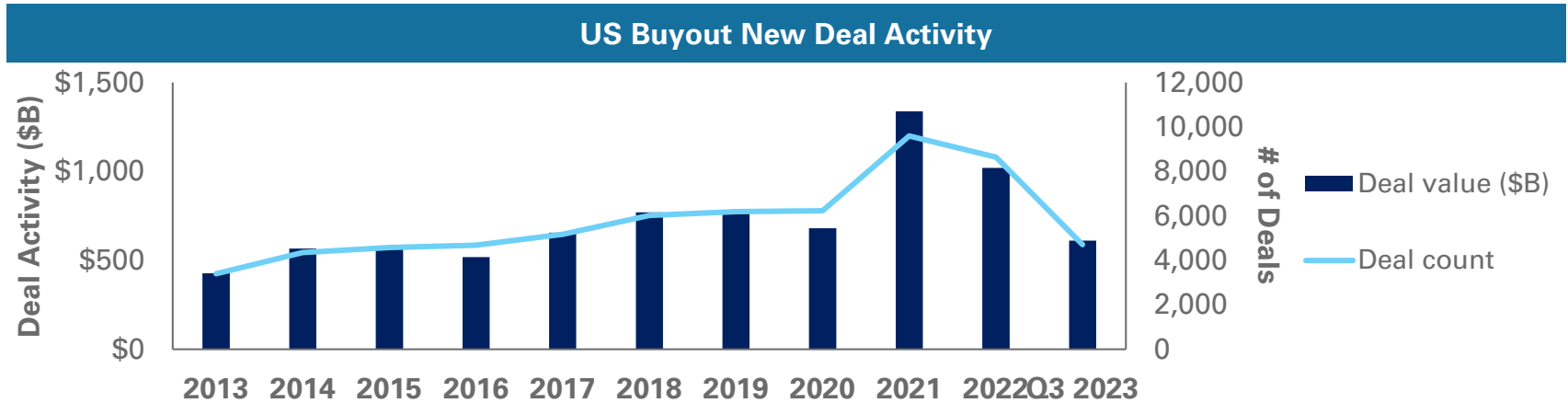


Source: Venture fundraising data from Q3 2023 Pitchbook NVCA Venture Monitor Report as of 09/30/2023. Venture dry powder data from Pitchbook Q3 2023 Pitchbook NVCA Venture Monitor Report as of 03/31/2023. Growth equity and buyout fundraising data from Pitchbook Q3 2023 US PE Breakdown Report as of 09/30/2023. Buyout dry powder data from Pitchbook Q3 2023 US PE Breakdown Report as of 03/31/2023.



PRIVATE EQUITY DEAL ACTIVITY

PRIVATE EQUITY ACTIVITY HAS SLOWED MEANINGFULLY



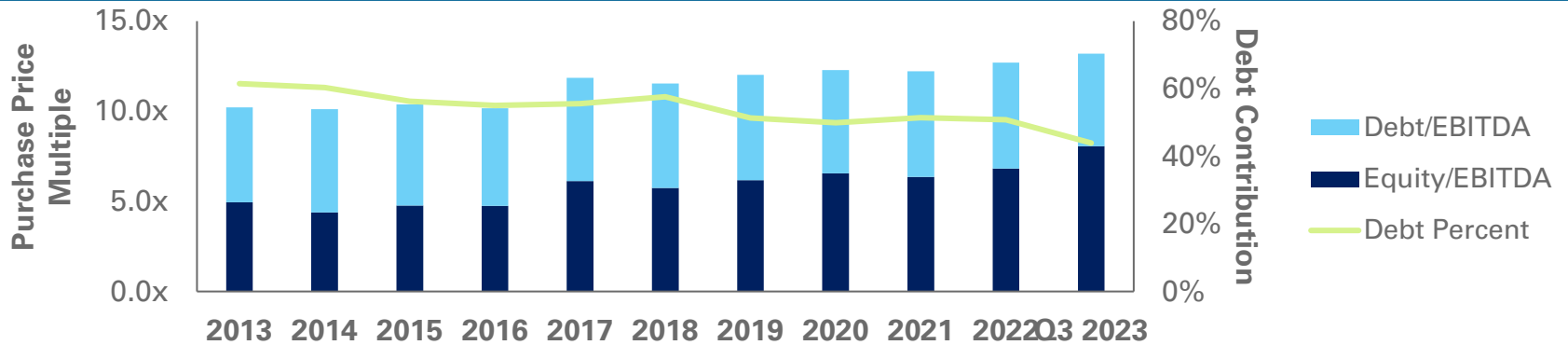
Source: Venture investment data from Q3 2023 Pitchbook NVCA Venture Monitor Report as of 09/30/2023. Growth equity and buyout investment data from Pitchbook Q3 2023 US PE Breakdown Report as of 09/30/2023.



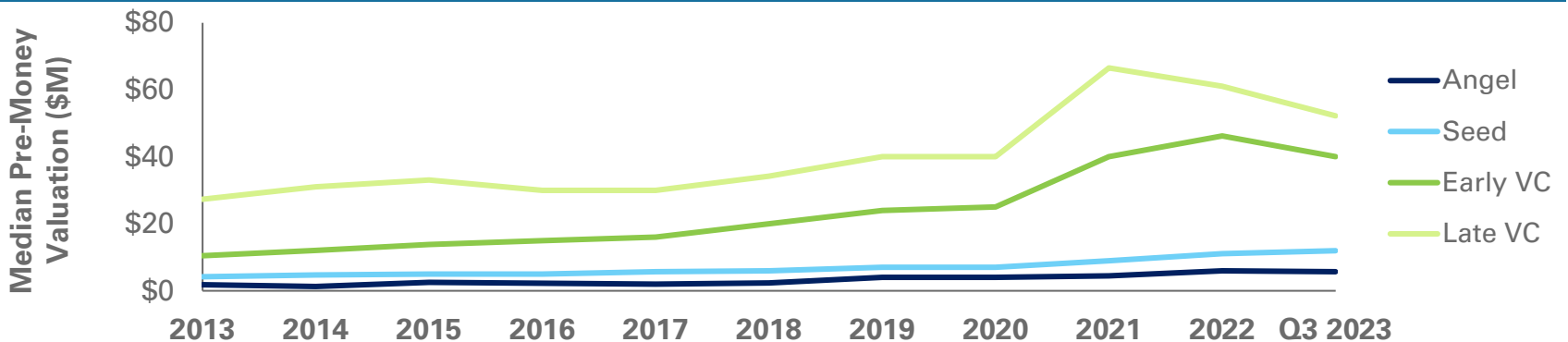
PRIVATE EQUITY VALUATIONS

VALUATIONS HAVE STALLED

US & Europe Buyout Valuations



US Venture Valuations

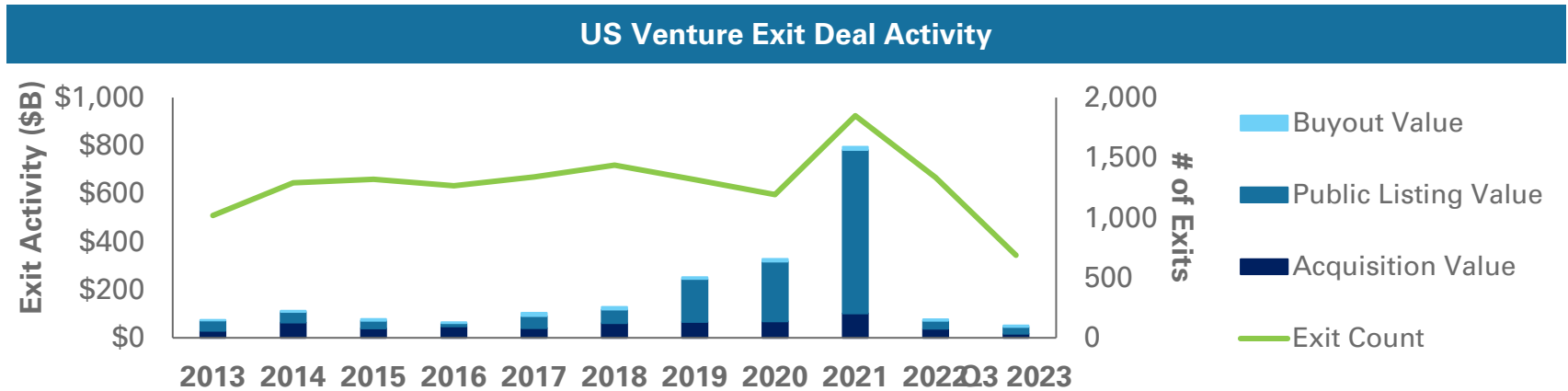
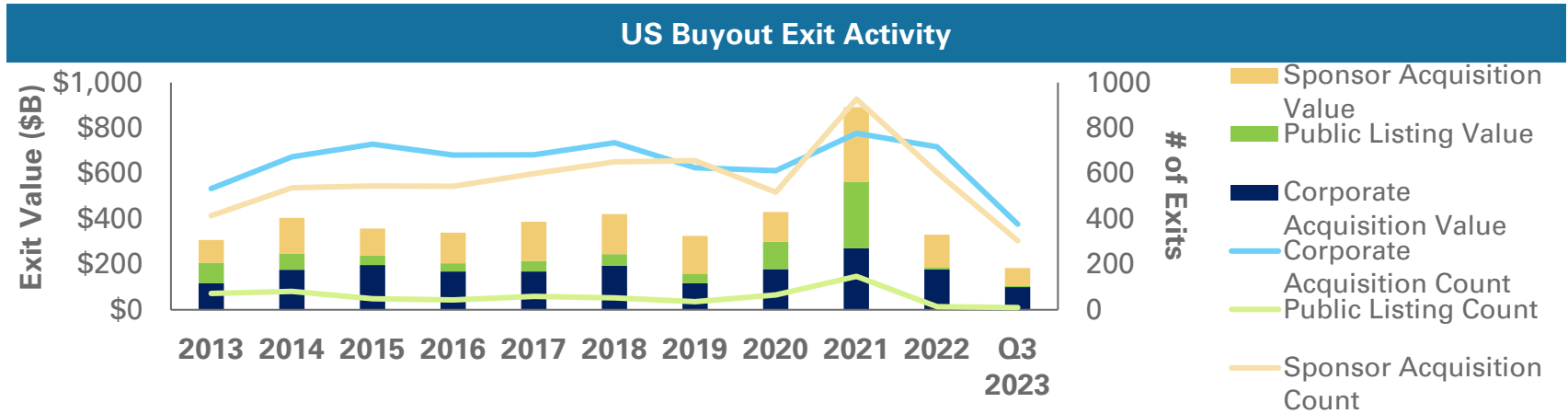


Source: Buyout valuation data from Pitchbook Q3 US PE Breakdown Report as of 09/30/2023.
 Venture valuation data from Q3 2023 Pitchbook NVCA Venture Monitor Report as of 09/30/2023.



PRIVATE EQUITY EXITS

EXIT ACTIVITY HAS PLUMMETED



Source: Buyout exit data from Pitchbook Q3 2023 US PE Breakdown Report as of 09/30/2023.
 Venture exit data from Q3 2023 Pitchbook NVCA Venture Monitor Report as of 09/30/2023.



THE BUYOUT OPPORTUNITY



PRIVATE EQUITY: VALUE INVESTING OPPORTUNITY

- Value is being able to buy an asset for less than the prevailing market price, or at a discount to what similar assets trade for.
- Investing for value can be challenging, especially when targeting high-quality companies—obviously, the competition for investment is high.
 - The last decade of ultra-low interest rates rewarded risk taking, high leverage, and growth at all costs, which led to an environment that ‘lifted all boats’. This left value strategies out of vogue.
- A higher rate regime is more conducive to value strategies and given that equity and debt valuations have traded down over the past year, more opportunities for value and even stress/distressed investing are emerging.



*Example of selected GPs that NEPC has underwritten who invest through a value-lens.

PRIVATE EQUITY: VALUE INVESTING

VALUE APPROACHES + WHAT TO LOOK FOR

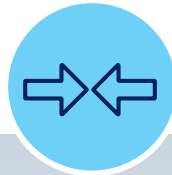
The basic premise of value-investing is buying a business where the purchase price is less than the intrinsic value

Watch out for the value trap!

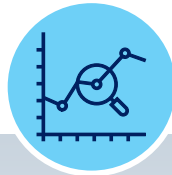
APPROACHES TO VALUE



Situational Complexities or 'Special Situations'



Contrarian Approach



Volatile Markets
Dislocation Between Perceived Value and Inherent Value



Partner of Choice



Lower-Middle Market

PRIVATE EQUITY: VALUE INVESTING

VALUE IN THE CURRENT ENVIRONMENT

The table below illustrates the impact of higher rates on private equity and why purchase price and low-leverage is a winning strategy across cycles.

	Value Buyer		Traditional Buyer	
	<i>Zero Rate Env.</i>	<i>Today</i>	<i>Zero Rate Env.</i>	<i>Today</i>
EBITDA Multiple	6x	6x	12x	12x
LTV (%)	50%	50%	50%	50%
Illustrative Interest Rate (%)	5%	10%	5%	10%
Cash Interest	\$3M	\$7M	\$7M	\$14M
Levered Post-Tax FCF	\$11M	\$9M	\$9M	\$2M
% of EBITDA	50%	38%	38%	8%

Hypothetical business converts less than 10% of its EBITDA into free cash flow, a reduction of ~80% vs. the same business in the prior, zero-rate environment.

*Note: \$23M EBITDA company with 15% EBITDA margin. Illustrative sales of \$150M & EBIT of \$20M. \$68M of debt for Value Buyer and \$135M of debt for Traditional Buyer. Assumes D&A/Main CapEx. Equal 2% Sales, 30% Tax Rate.

APPENDIX

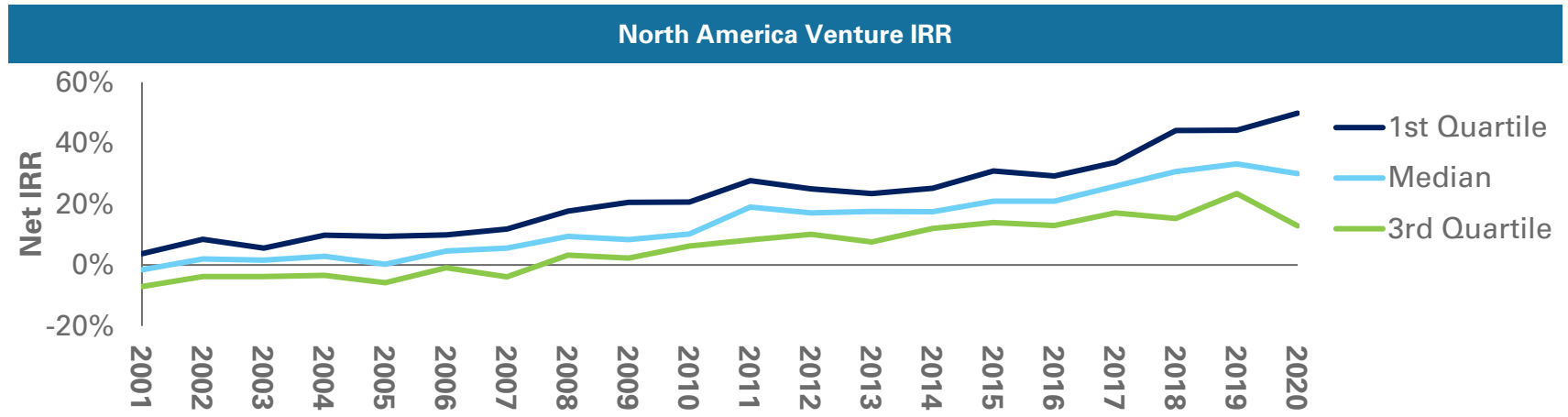
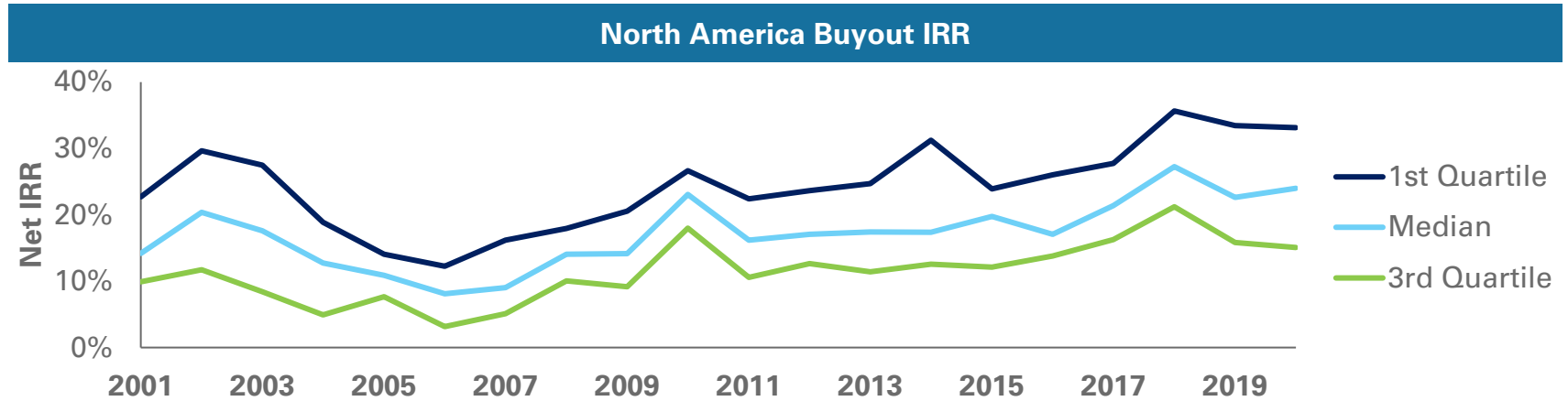


2024 PRIVATE EQUITY THEMES

Theme	Overview	Merits	Risks	Implementation
Free Cashflow Matters	Strategies are shifting from growth at any cost to a balanced emphasis on growth with a keen focus on cash flow management	Cost of leverage has increased significantly No longer an “L” BO market – strictly Buy Out	Leveraging is becoming costlier, necessitating companies to uphold sufficient cash reserves to meet interest expenses. Return expectations are anticipated to decrease.	Benefits to Client Portfolios <ul style="list-style-type: none"> Return enhancement Strategy Options <ul style="list-style-type: none"> Distressed/stressed Special situations
Competitive Landscape Consolidation	A shift toward quality, evident in a decline in the number of funds being raised from recent historic highs	Sharp decline in the number of funds being raised from recent historic highs	Anticipated challenges for some managers in raising capital, especially high fundraising risk for newer entrants	Benefit to Client Portfolios <ul style="list-style-type: none"> Return enhancement Accessing high-quality managers as Limited Partners reduce their commitments Strategy Options <ul style="list-style-type: none"> Early-stage venture LMM Buyout
Valuations are coming back to earth	Foresee continued downward pressure on both buyout and venture pricing throughout 2024	As companies deplete their cash reserves, management teams are likely to recognize that current valuations represent a significant discount compared to the previous 24 months.	Anticipate devaluations for existing investments	Benefit to Client Portfolios <ul style="list-style-type: none"> Return enhancement Strategy Options <ul style="list-style-type: none"> LMM Buyout Venture Secondaries

PRIVATE EQUITY RETURNS

ATTRACTIVE VINTAGE YEAR RETURNS



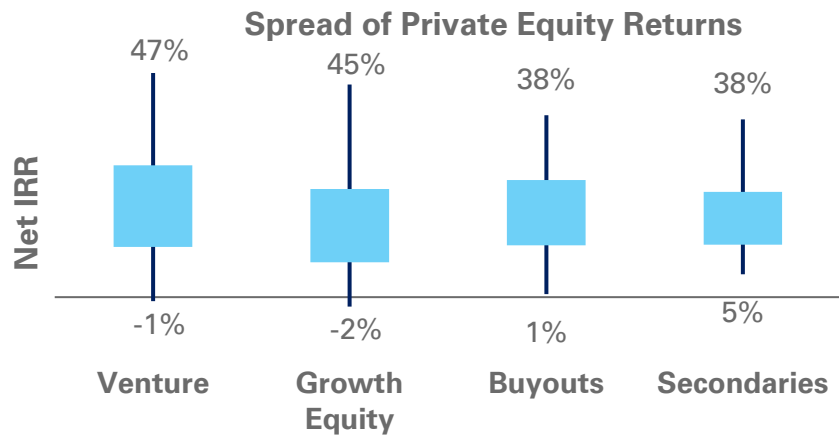
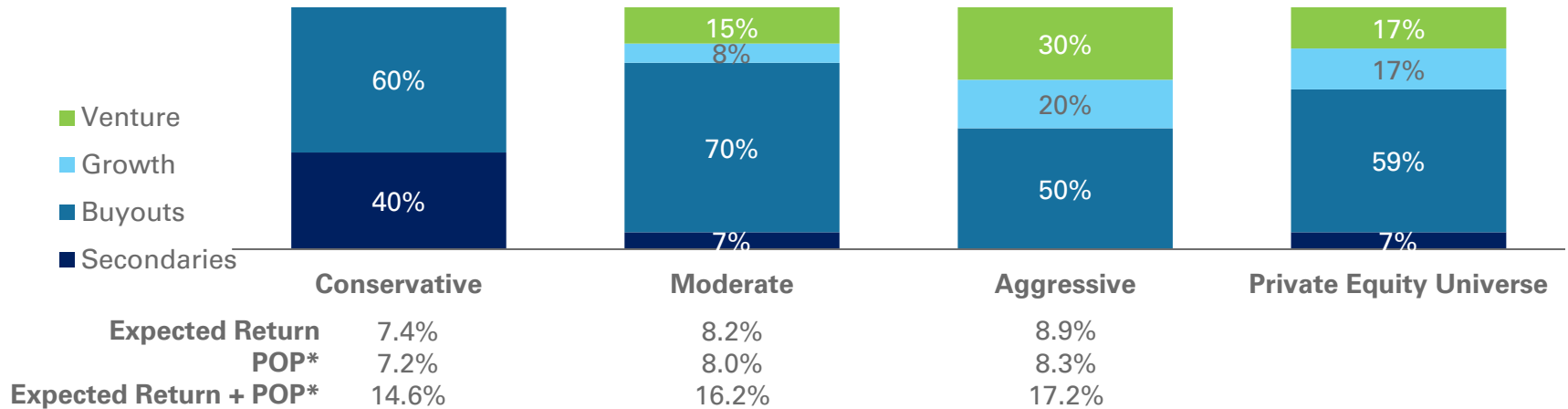
Source: Thomson One/CJA as of 06/30/2023. Performance for most recent vintage funds not yet meaningful.



PRIVATE EQUITY BEST PRACTICES

- **Strategic targets are encouraged but don't be dogmatic**
- **Pacing plans are a critical portfolio management and risk management tool**
- **Private Equity is a long-term investment and should not be used express tactical investment views**
- **Re-up with strong managers**
- **Ensure overall asset allocation has enough true liquidity to meet calls and spending**
- **If you are early in your private equity investment journey, or building out a larger allocation, know that it will take time**

PRIVATE EQUITY MODEL PORTFOLIOS



	Check Size	POP*
Venture	1.0%	900 bps
Growth	1.25%	800 bps
Buyouts	1.5%	800 bps
Secondaries	2.0%	600 bps

Source: NEPC, CJA. Private Equity Universe represents market cap of funds raised and invested from 2013-2022. Net IRR spread calculated as pooled 10-yr IRR through 2019. Vertical lines represent 5th percentile (top) and 95th percentile (bottom). Blue bars represent spread between 25th and 75th percentiles. Check size is a % of the total client NAV. Fund of Fund allocations are included in relevant strategy types (LBO, VC, etc). Expected return reflects NEPC capital market assumptions as of 6/30/23.

*Potential Out-Performance: upside potential from strong manager selection (25th percentile to 50th percentile spread)



NEPC DISCLOSURES

Past performance is no guarantee of future results.

All investments carry some level of risk. Diversification and other asset allocation techniques do not ensure profit or protect against losses.

Some of the information presented herein has been obtained from external sources NEPC believes to be reliable. While NEPC has exercised reasonable professional care in preparing this content, we cannot guarantee the accuracy of all source information contained within.

The opinions presented herein represent the good faith views of NEPC as of the publication date and are subject to change at any time.

This presentation contains summary information regarding the investment management approaches described herein but is not a complete description of the investment objectives, portfolio management and research that supports these approaches. This analysis does not constitute a recommendation to implement any of the aforementioned approaches.



ALTERNATIVE INVESTMENT DISCLOSURES

It is important that investors understand the following characteristics of non-traditional investment strategies including hedge funds and private equity:

1. Performance can be volatile and investors could lose all or a substantial portion of their investment
2. Leverage and other speculative practices may increase the risk of loss
3. Past performance may be revised due to the revaluation of investments
4. These investments can be illiquid, and investors may be subject to lock-ups or lengthy redemption terms
5. A secondary market may not be available for all funds, and any sales that occur may take place at a discount to value
6. These funds are not subject to the same regulatory requirements as registered investment vehicles
7. Managers may not be required to provide periodic pricing or valuation information to investors
8. These funds may have complex tax structures and delays in distributing important tax information
9. These funds often charge high fees
10. Investment agreements often give the manager authority to trade in securities, markets or currencies that are not within the manager's realm of expertise or contemplated investment strategy

