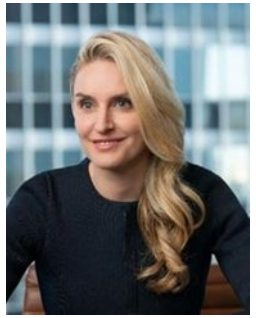
Private Equity Market Trends

A Spotlight for IBA New York

June 6, 2023

Panelists

Co-Chairs:



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Commentator:

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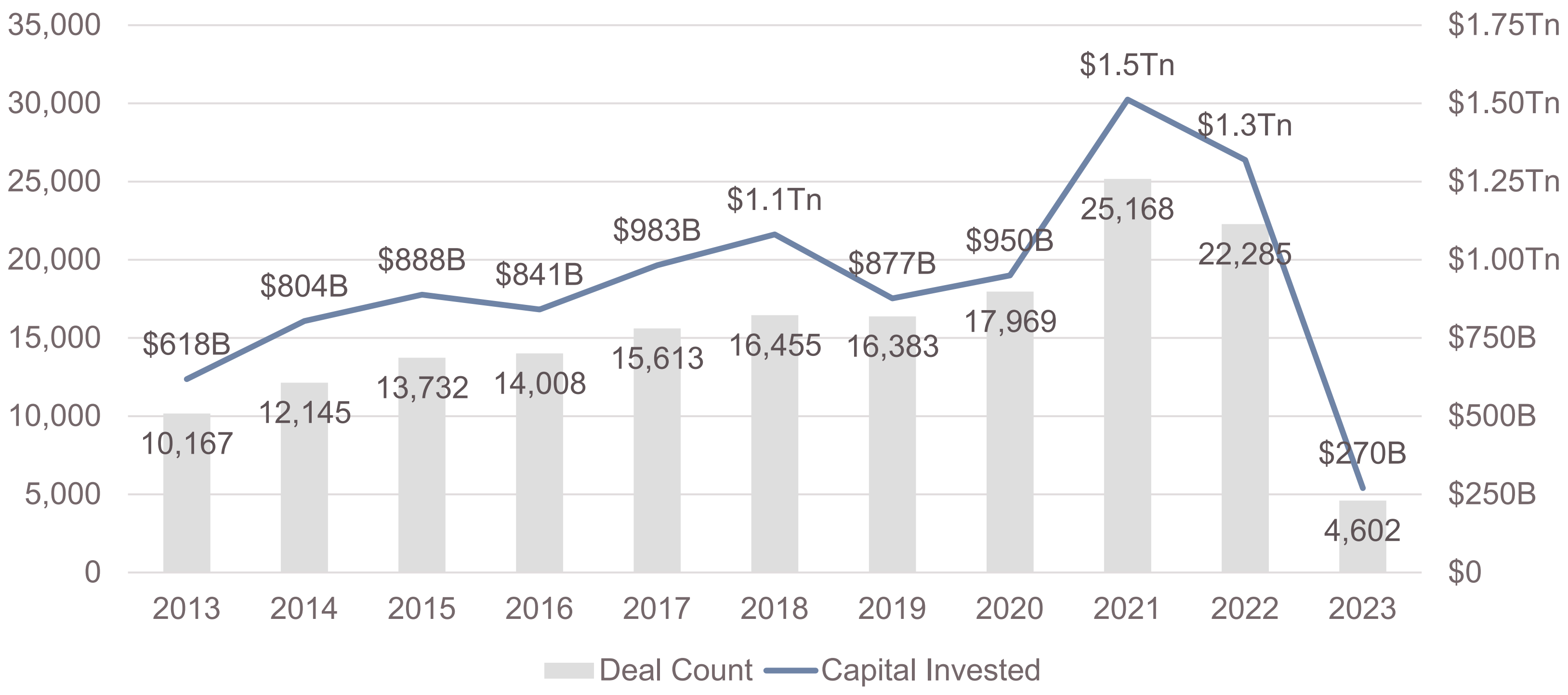
Overview of the Market

After record-breaking levels of PE deal activity and capital invested in 2021, 2022 – while lower – was still the second most active year in history. 2021 was also notable in that we were seeing, on average, larger deals as a percentage of overall deals completed. Early indications suggest that deal activity, average size and capital invested will return to lower, pre-pandemic levels in 2023.

Global PE Deal Count & Capital Invested 2013 – Q1 2023



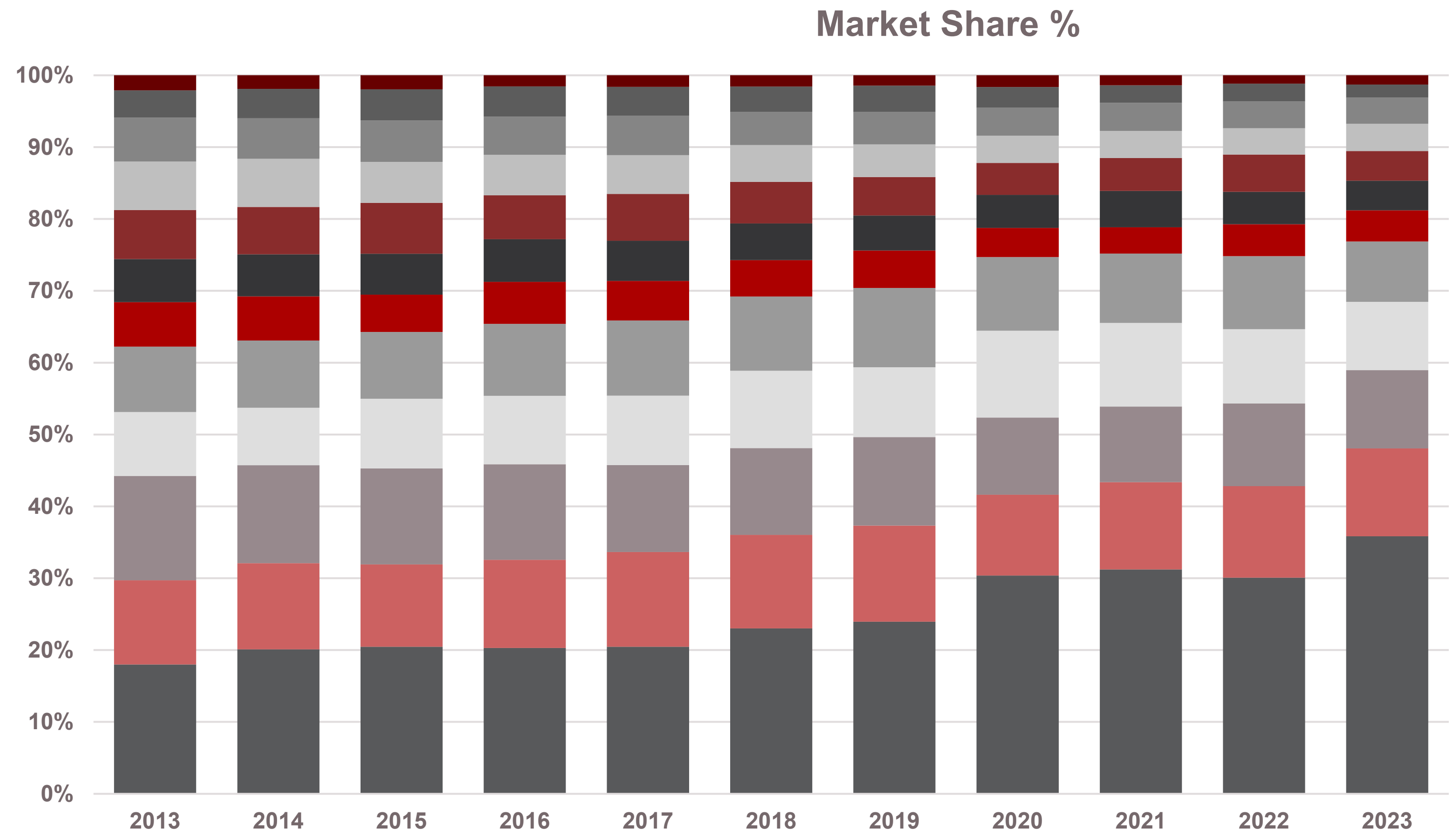
	2020	2021	2022	2023*
Under $25M	66%	60%	61%	66%
$25-$100M	16%	18%	17%	15%
$100-$500M	12%	16%	15%	13%
$500M-$1B	3%	3%	3%	3%
$1B – 2.5B	2%	2%	3%	2%
2.5B+	1%	1%	1%	1%

Source: Pitchbook Data

Overview of the Market

Sector focus has remained relatively consistent over time, with the exception of technology where we have seen an increase of 10% from 2015 levels. This sector should continue to gain momentum as technology expands into other major sectors such as finance and healthcare.

Global Buyout Deal Count, by Sector



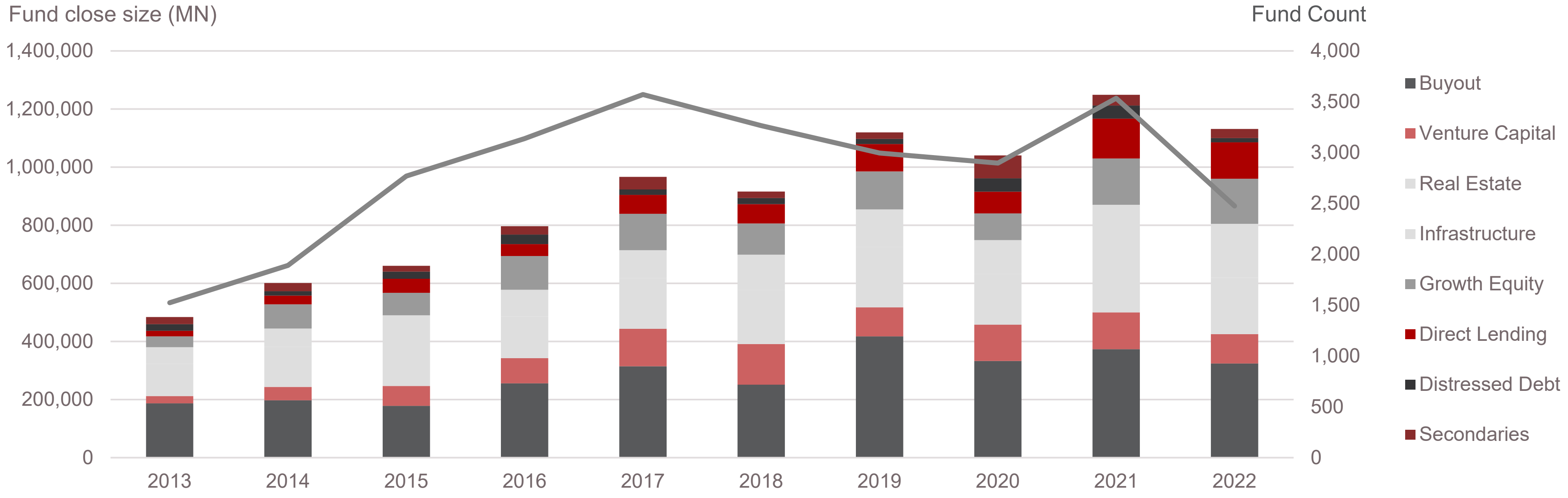
	2015	2020	2021	2022
Telecommunications	2%	2%	1%	1%
Real Estate	4%	3%	2%	2%
Consumer Staples	6%	4%	4%	4%
Materials	6%	4%	4%	4%
Media and Entertainment	7%	4%	5%	5%
Retail	6%	5%	5%	5%
Energy and Power	5%	4%	4%	4%
Financials	9%	10%	10%	10%
Healthcare	10%	12%	12%	10%
Industrials	13%	11%	10%	12%
Consumer Products and Services	12%	11%	12%	13%
High Technology	20%	30%	31%	30%

Notes: Excludes add-ons; excludes loan-to-own transactions and acquisitions of bankrupt assets; based on announcement date; includes announced deals that are completed or pending, with data subject to change
Source: Refinitiv

Overview of the Market

Global fundraising reversed course in 2022, but the total raised was still the second highest ever. The total number of buyout funds closed in 2022 skidded 46% from 2021 as most firms found it increasingly difficult to raise new capital. The five-year fundraising total still reached a staggering $5.5 trillion, dwarfing any five-year period in the industry's history.

Global private capital raised, by fund type ($M)

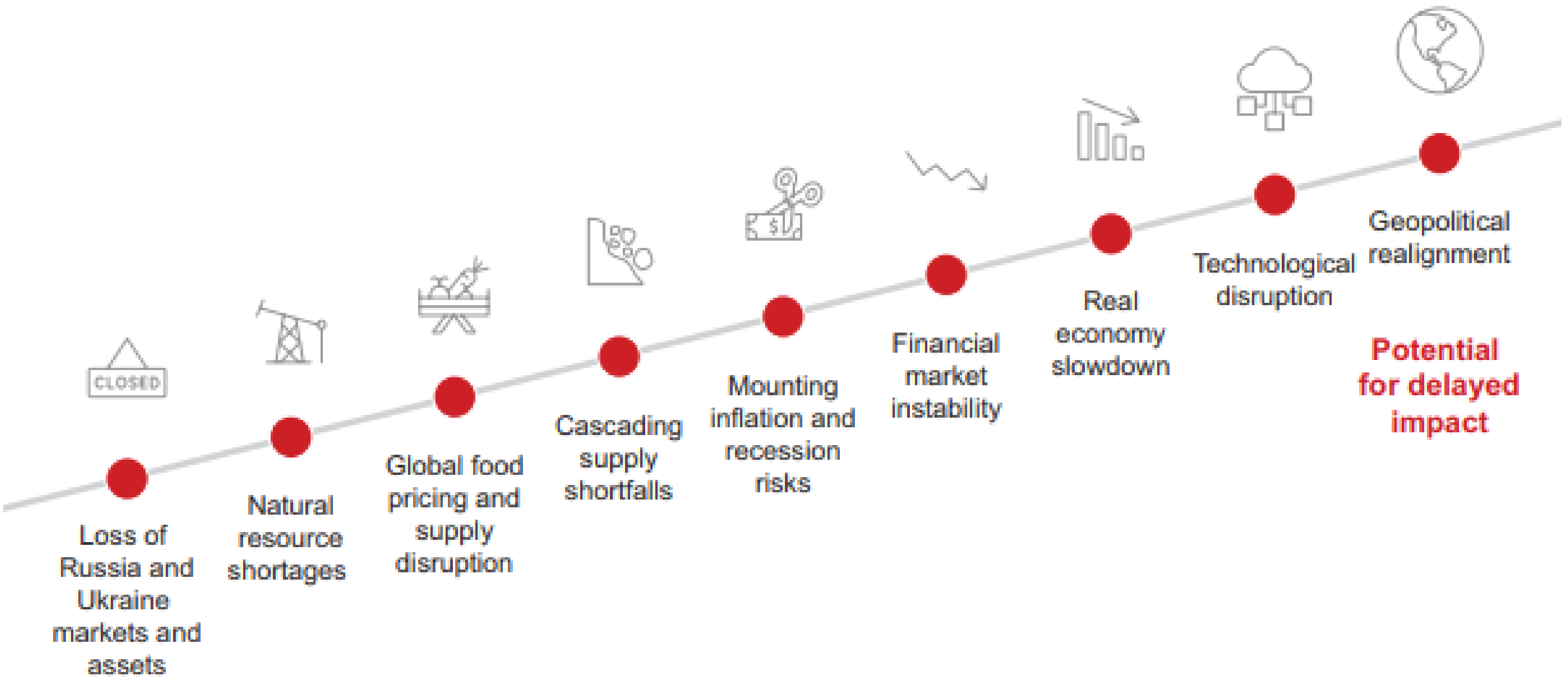


2015	2020	2021	2022
27%	32%	30%	29%
10%	12%	10%	9%
25%	17%	18%	17%
12%	11%	11%	16%
12%	9%	13%	14%
7%	7%	11%	11%
4%	4%	4%	1%
3%	8%	3%	3%

Source: Preqin

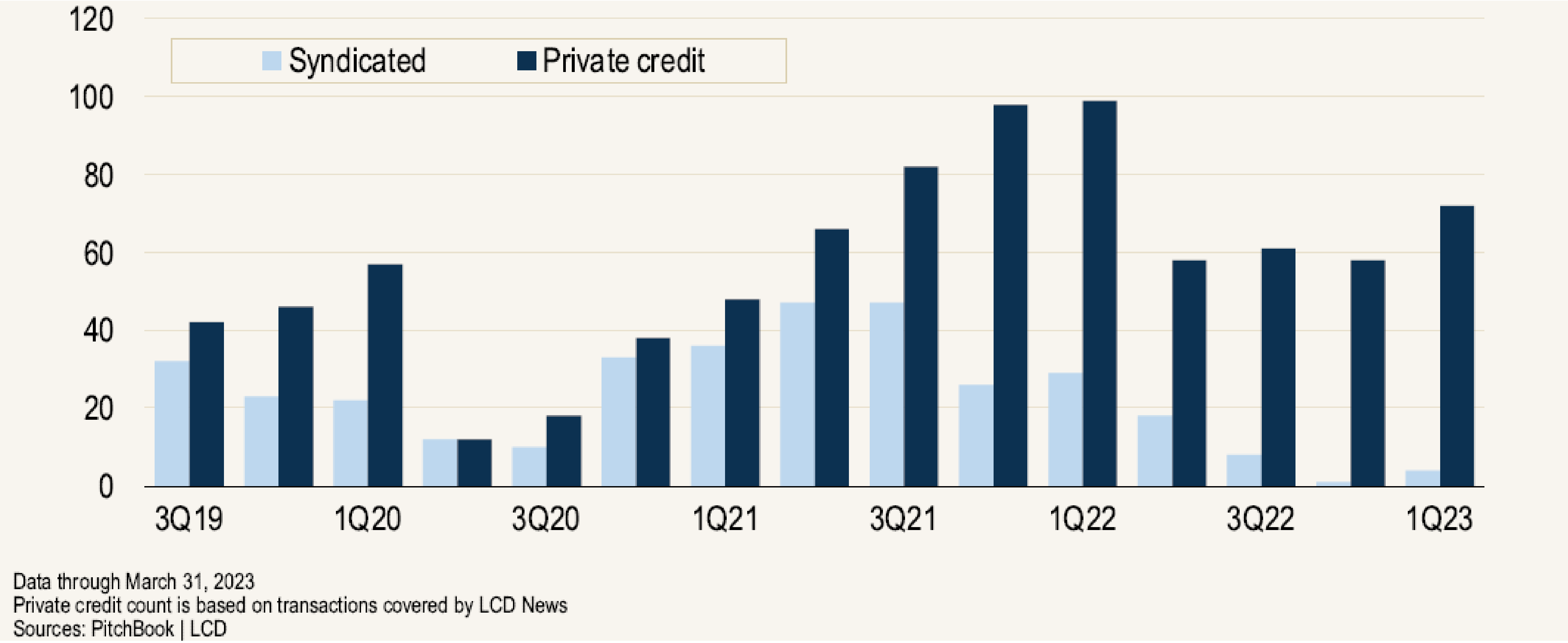
Overview of the Market

The macro environmental has posed a range of significant challenges



Source: Bain & Company, Global Private Equity Report 2023

Overview of the Market



Count of LBOs Financed in BSL vs Private Credit Markets

Source: Bain & Company

Overview of the Market

With higher interest rates and banks becoming more cautious in their lending practices, PE players are looking for novel capital development strategies. Lower-middle market LBOs are still being, but larger LBO have been challenged.

Novelty deal characteristics include:

- Deals with less leverage
- Larger equity checks
- Rise of Direct Lending
- Continuation Funds

REUTERS®

Analysis: Banking turmoil takes the leveraged out of the buyout

March 23 (Reuters) - Private equity firms that acquired companies since the banking crisis started on March 8 have funded the deals mostly with their own funds, a departure from traditional leveraged buyouts that reflects their struggle to secure cheap debt.

PitchBook

Banking crisis puts pressure on PE money supply

pwc

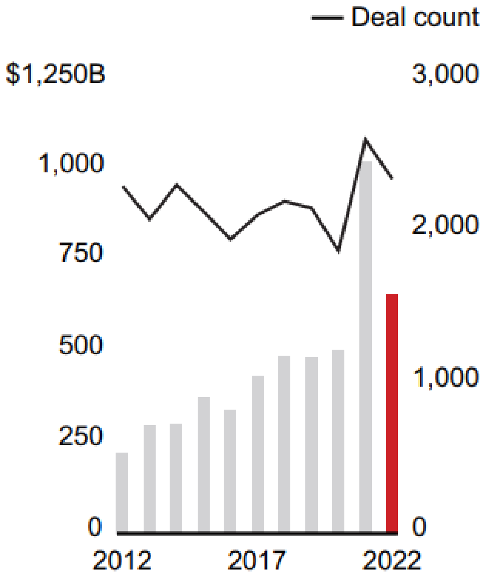
"We're in a period of intense change for PE, reflecting the acute economic environment and longer-term evolution. Success requires both navigating near-term uncertainty and positioning for future differentiation through talent, digital and ESG" – Manoj Mahenthiran, US PE Deals

Trends of Private Equity Markets in 2023 and Beyond

The End of Up Cycle since 2010, the Growth is On Pause in 2023

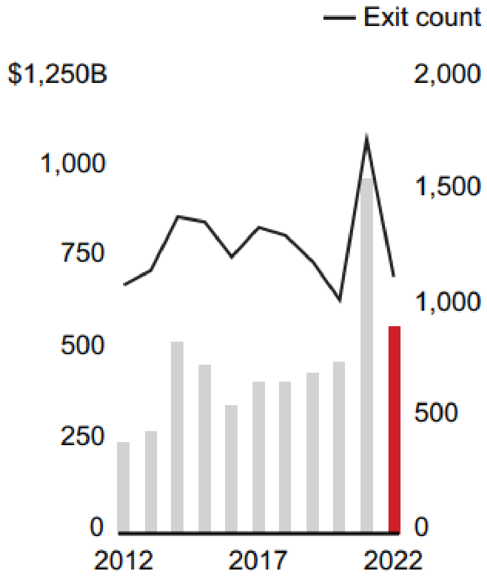
Investments

Global buyout deal value



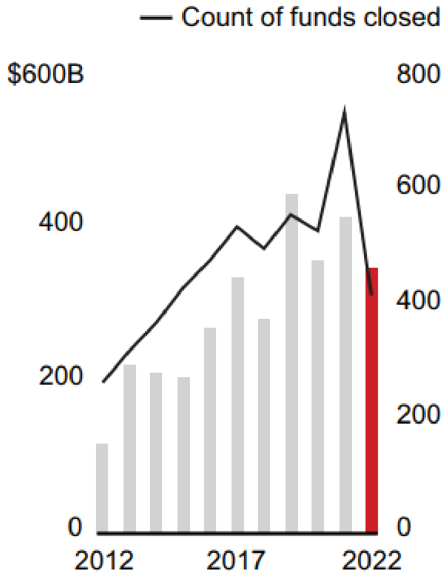
Exits

Global buyout-backed exit value



Fund-raising

Global buyout capital raised



Notes:
Investments—excludes add-ons; excludes loan-to-own transactions and acquisitions of bankrupt assets; based on announcement date; includes announced deals that are completed or pending, with data subject to change; Exits—includes full and partial exits, bankruptcies excluded; IPO value represents offer amount and not market value of company; Fund-raising—data grouped by the year in which funds held their final close; count is of all funds, including those for which final close data is unavailable; buyout category includes buyout, balanced, coinvestment, and coinvestment multimanager funds; excludes SoftBank Vision Fund

Sources: Dealogic; Preqin; Bain analysis

- Global events-Pandemic, lock-down country by country, disrupted economy activities/supply chain and diminished income, however Covid polices/packages had to be delivered through central banks to “print money” to finance fiscal shortfalls
- Monetary policies of central banks to curb the inflation, reduced future value due to rising interest rates, investor recalibration, GP conservatism, etc, lead to the investments blues, exits drop/IPO door shut, fund-raising tap out, return fell, etc.
- Other various macro-factors.

Source: Bain & Company

Trends of Private Equity Markets in 2023 and Beyond

- **Gloomy Market with Some Sunny Spells**
  - Growth was down or muted across many sectors, technology still accounted for almost 1/3 of global buyout deals;
  - The trend away from generalist funds and to specialization: infrastructure still holds up
  - Energy transition, a revolutionary opportunity opening up potential investment across the global economy.
- **Positive Outlook for Private Equity**
  - Much more resilient than the public markets in last 20 years
  - Deep dive to the massive sovereign wealth funds and individual wealth
  - Adopt both offense and defense strategies in the portfolio by investing in automation, supply chain redundancy and security, etc.

Deal Characteristics

Keeping Score

- Q12023 deals worth US$92bn v US$240 in Q1 2022
- Decrease in multiples creating opportunities

Looking for Leverage

- In Q1 in EMEA, only one deal >5bn, and 6 >1bn
- >80% of PE deals by value in 2023 have been P2P

Corporate Capacity

- Liquidity / activism / ESG driving divestments
- Strategics constrained by reduced finance capacity

Technology Bust?

- Volumes down in 2022, but remains significant focus
- 80% in Q1 in software vertical

ESG Again!

- Focus on “picks and shovels” – enabling tools and tech
- ESG impact on corporates and PE

No Exits…

- Lack of IPO market, muted appetite from strategics
- Add-on / buy-and-build focus

Deal Characteristics

Deal types and trends

- GP-led secondaries / Continuation Funds:
  - With the recent tailwinds in IPOs, sponsors are looking at alternative exits including through GP led secondaries and continuation funds.
  - GP-led secondaries are becoming increasingly popular globally and in APAC markets as a solution for liquidity concerns and 'right valuation' for crown jewel assets.
  - GP-led secondaries market has grown tenfold – from $5 billion (in 2013) to $50 billion (in 2022).
  - Key to find a pricing that works for the exiting investors but keeps the acquisition attractive for the incoming investors.
  - Equity market investors are becoming increasingly vocal about: (i) how private markets value companies; (ii) who controls the investment committee between LPs and GP; and (iii) any safeguards that can be built to avoid 'self-dealing' concerns (e.g., third-party valuations)?
  - India has a tightly regulated funds regime which poses issues for such GP-led secondaries.
- Classic LBO: Yet to evolve in India but shift in outlook of promoters / founders being now open to give away control – significant move for buyout firms.
- Take Private (P2P): Global boom for P2P deals amidst equity bear markets. Remain less common in India as compared to other jurisdictions due to overlapping regulations, pricing uncertainty, approval uncertainty and potential sell down risks.
- Bolt-on / Add-ons: As buyouts remain harder to come by, bolt-ons / add-ons, buy and build deals and corporate carve-outs are on the rise.
- Control deals: Increase in control deals over the last few years (both public and private). Discussions become complex where target has multiple investors with different horizons / objectives / exit timelines.

Deal Terms and Considerations

Closing/termination recourse

- Deal certainty through

  >Full equity backstop

  –a powerful tool in "hot auctions" for PEs vs. strategic buyers

  –in Europe "certain funds" bank financing or "fund-level debt facilities" are more commonly seen

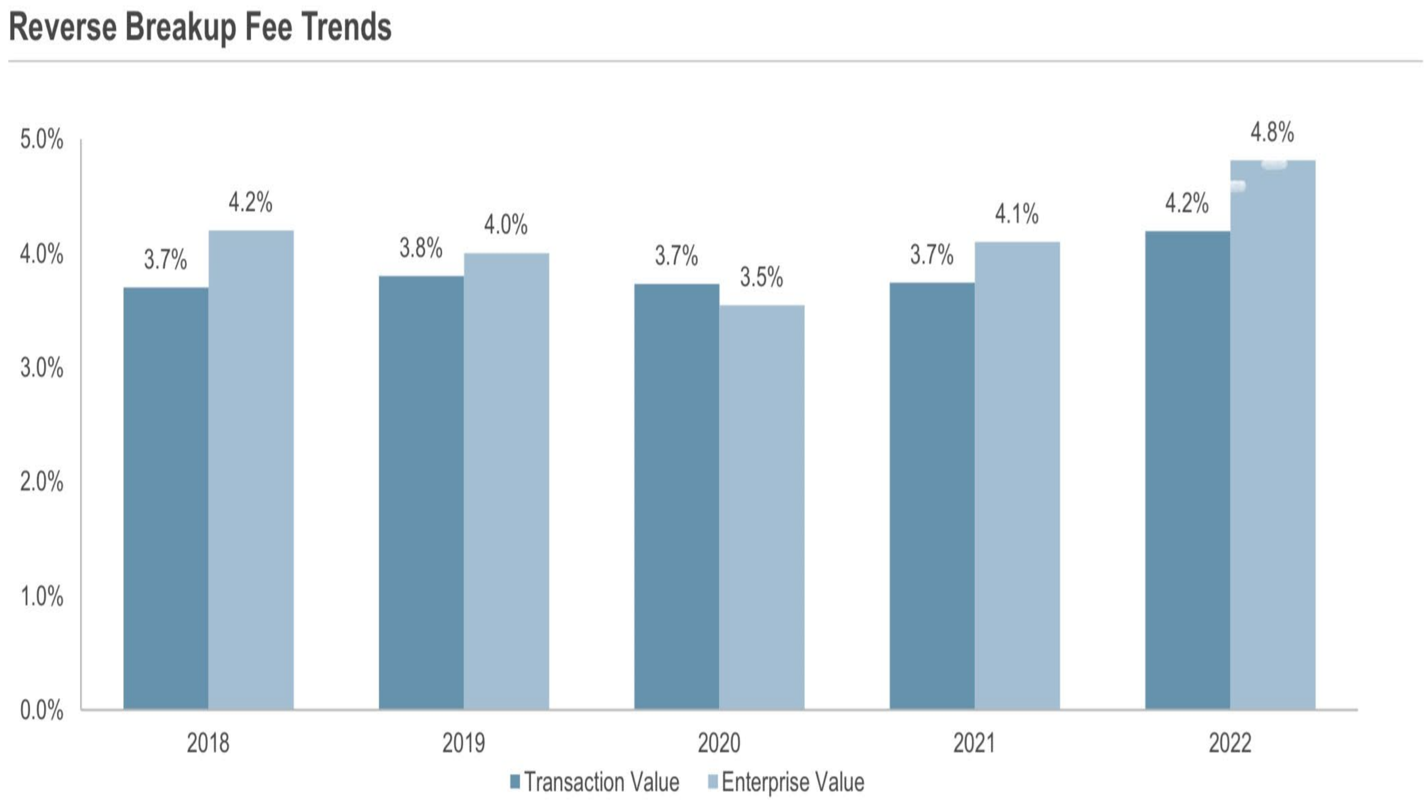
  > Reverse termination fees

  – between 3.7% and 4.8% of total transaction value

  – in Europe more commonly used if there is an antitrust/ regulatory concern/conditionality

Closing conditionality

- Different approach to closing conditions in the US and Europe
- MAC clauses seen also in European deals due to geopolitical crisis and price volatility
- Re-thinking of "hell-or-high-water" clauses



– Source: Houlihan Lokey 2022 Transaction Termination Fee Study http://cdn.hl.com/pdf/2023/2022-transaction-termination-fee-study.pdf)

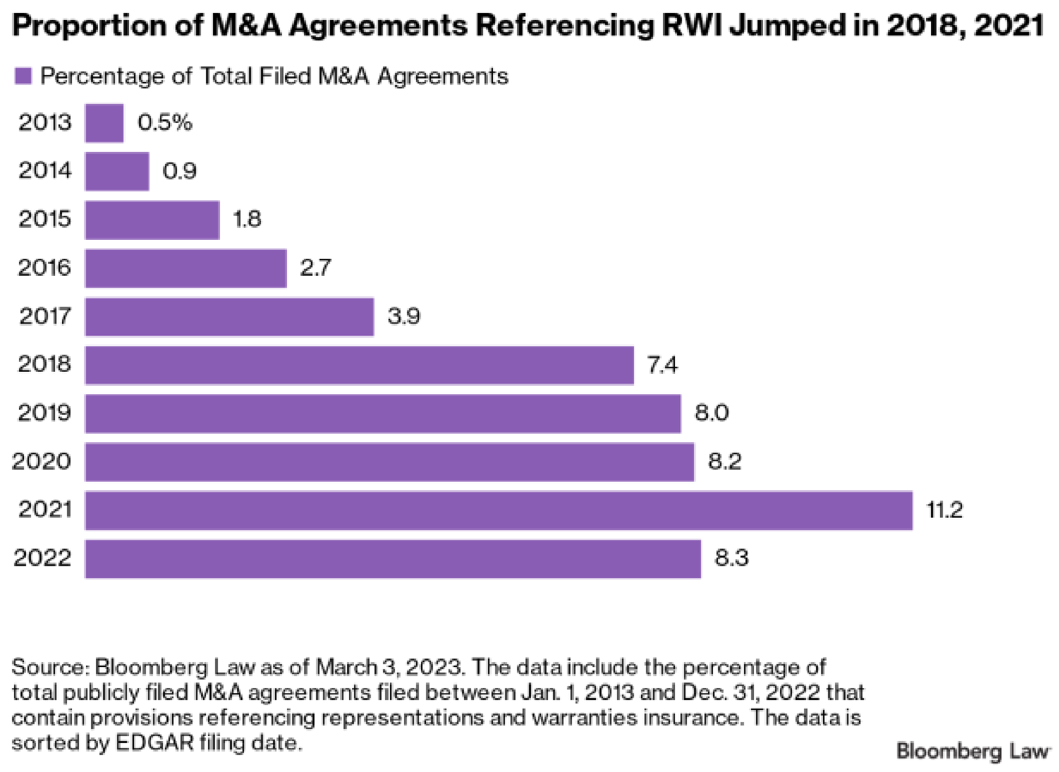
Deal Terms and Considerations

Post closing recourse

- RWI fairly pervasive (all sort of deals and industries) and "evolved"
- Commonly with "no seller recourse/nil recourse" structure (in the absence of fraud). "No skin in the game" generally accepted by insurers
- Being fraud the only remedy, defining it properly is key

Scope of reps/warranties

- More robust set of R&Ws with RWI
- Management R&Ws vs. sellers' R&Ws



Deal Terms and Considerations

Impact of ESG

- R&Ws added or expanded to address specific ESG issues
  - > Compliance with laws and data privacy representations to cover also industry standards, best practices or other soft laws (e.g. "*The Seller has no knowledge of situations, events or conditions at the target company from the areas environmental, social or governance (ESG), which, within the past [•] years before the signing date, have existed or occurred in violation of laws, regulations or standards which is reasonably expected to have a material adverse effect on the target company's assets, financial and earnings situation or on the target company's reputation*").
  - > #MeToo representations and warranties or "Weinstein clauses"
- Performance targets and earn-out provisions linked to ESG
- Covenants to take steps post-closing to enable compliance with ESG disclosure requirements
- ESG-Linked Acquisition Financings

Regulatory Hurdles: Antitrust/Competition Law: US

The Deal **Feds Slow-Walk Private Equity Transactions**

Once-routine combinations that easily cleared past administrations during the initial 30-day review window under the Hart-Scott-Rodino premerger notification regime are drawing rigorous attention from antitrust officials suspicious of the business motives of buyout shops.

THE WALL STREET JOURNAL.

Antitrust Regulators Fix Their Sights on Private Equity

Tougher antimonopoly enforcement in Washington is complicating buyout firms' efforts to close acquisitions

Increased Agency Enforcement and Private Equity Focus

- FTC Chair Kahn has expressed that private equity may be unhealthy for competition and therefore that private equity deals merit special focus.
  - "Antitrust enforcers must be attentive to how private equity firms' business models may in some instances distort incentives in ways that strip productive capacity, degrade the quality of goods and services, and hinder competition."
  - "[S]erial acquisitions or 'buy-and-buy' tactics can be used by private equity firms and other corporations to roll up sectors, enabling them to accrue market power and reduce incentives to compete, potentially leading to increased prices and degraded quality."

— FTC Chair Lina Khan, June 13, 2022

Regulatory Hurdles: Antitrust/Competition Law: US

Increased Antitrust Enforcement in 2023

- FTC and DOJ continue to expand their approach to antitrust enforcement, including “reactivating the full set of authorities that Congress granted” the agencies and “updating [their] tools to ensure they better correspond to new market realities.”
- The agencies have expressed a desire to prioritize swift enforcement action over playing it safe, and voiced a willingness to lose in litigation to advance antitrust case law.

Second Requests Increasing in Scope

- High number of Second Requests
- Harder line on Second Request compliance
- Expanded scope of Second Requests
  - Acquisition pipelines, tuck-ins, and add-ons
  - Focus on effects on employees, other stakeholders
  - Requests directed to private equity firms themselves

Regulatory Hurdles: Antitrust/Competition Law: US

Reinvigorated Enforcement of Interlocking Directorate Violations

- FTC and DOC have indicated intent to strengthen enforcement of the prohibition against interlocking directorates – *i.e.,* situations where a person simultaneously serves on the board of two or more competing corporations.
    - This issue is especially relevant to private equity firms' corporate governance of portfolio companies.
- The agencies have historically taken action against interlocks in the context of premerger investigations during HSR review, but are now signaling an intent to pursue interlocks outside of the HSR review process.
    - A few months ago, the FTC took steps to make it easier for the Commission to issue subpoenas and civil investigative demands in investigations relating to interlocking directorates, stating that such interlocks "continue to raise significant competitive concerns."
- Whereas voluntary resignation of a director has previously been sufficient to address an interlock violation, moving forward the agencies may seek prospective injunctive relief as well as fines or other penalties against offending companies.

Regulatory Hurdles: Antitrust/Competition Law: EU/UK

EU – 2022 more aggressive enforcement hasn't translated into fewer deals cleared

- 371 transactions notified, of which more than 90% cleared unconditionally in Phase 1.
  - 2 prohibitions; 12 deals abandoned/ withdrawn

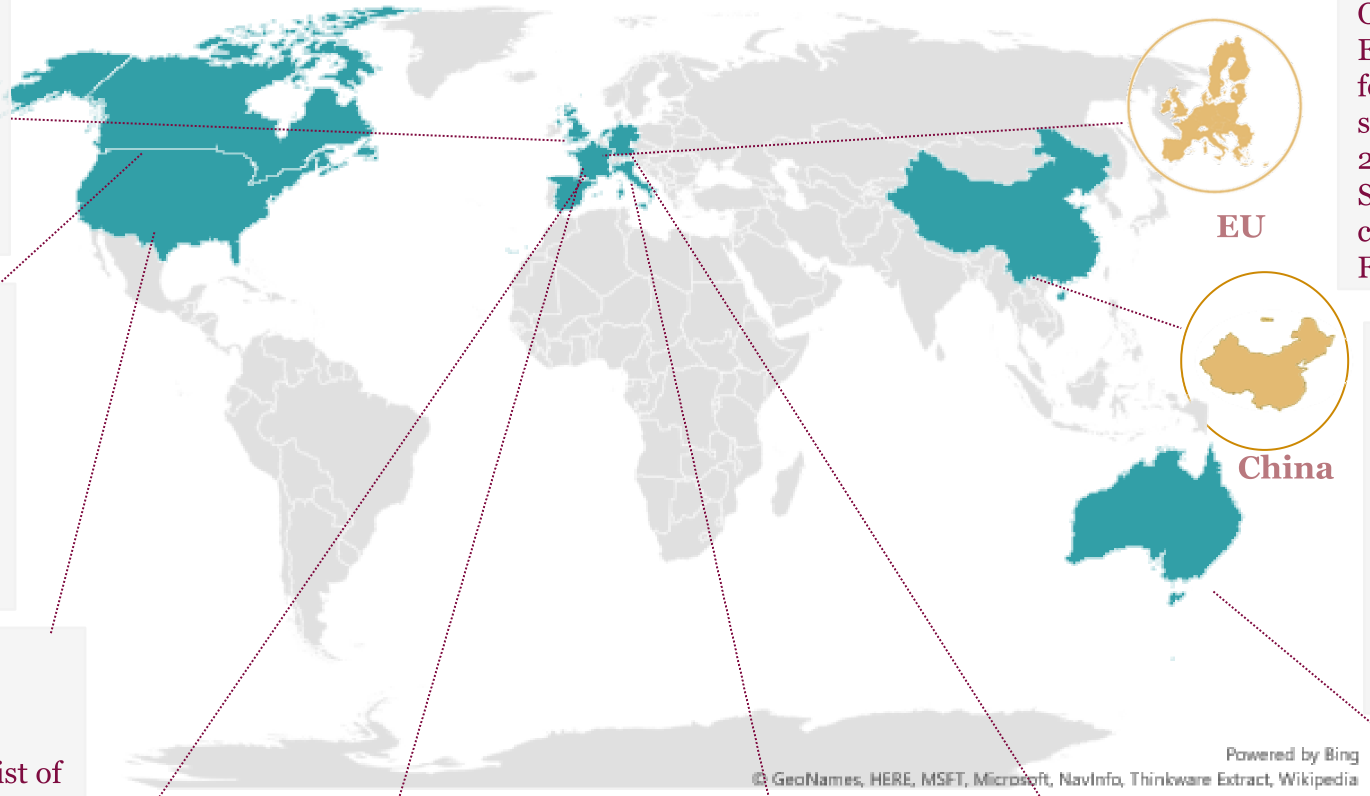
UK – continued to be one of most aggressive authorities with occasionally divergent outcomes

- 43 decisions in the last year, of which almost 50% were conditionally cleared or blocked.
  - 18 remedies; 3 prohibited, plus 5 abandoned.

Overall trend of enhanced scrutiny has knock-on effect on deal timeline and closing

- Tech deals in particular continue to be a main focus in the EU and UK.
- Not the same spotlight on PE deals in the EU and UK as in the US!
  - However the UK CMA has been looking at consumer facing roll-ups in sectors such as dental and veterinary and has noted the PE-linked levels of debt.
- Antitrust authorities increasingly get creative to review deals that arguably do not qualify as they fall below the thresholds, (e.g.) *Illumina/GRAIL.*
- Timelines are getting longer and less predictable because of multiple reviews and more scrutiny across more jurisdictions.
  - Upward trend of deals being abandoned more often than prohibited because of enhanced regulatory scrutiny, (e.g.) *NVIDIA/Arm*.
- Overall, a more complex and muddled regulatory environment is leading to foot-faults and fines as companies try to get the jump on pre-integration planning prior to closing

Regulatory Hurdles: Increased FDI focus due to global events (e.g. Covid 19, Russian invasion of Ukraine)



UK

UK National Security & Investment Act came into force in January 2022 (retrospective to November 2020)

Canada

2020: Policy statement that all FDI will be scrutinized; 2021: monetary thresholds lowered; 2022: voluntary regime introduced

USA

Feb 2020 Financial Investment Risk Modernization Act expanded CFIUS. List of critical technologies updated Feb 2022

Spain

Enhanced temporary measures are in place until December 2024 (since 2020). Draft legislation has been published to implement the temporary measures as permanent.

France

New FDI regime finalized April 2020. Temporary threshold reduction for listed companies extended until December 2023.

Italy

“Temporary measures” in place during Covid and until end of 2022 formalized in new permanent regime from 1 January 2023

Germany

May 2021 Amended FDI regime to include 16 new mandatory notification sectors. In January 2022, expansion of critical infrastructure operators definition.

Australia

From 1 January 2021, all foreign investments that raise national security concerns require approval. Fees were increased in July 2022.

EU

October 2020 New EU regulation on foreign investment screening. As of May 2023, only 2 Member States have no current or planned FDI regime.

China

January 2021 Issued Measures for Security Review of Foreign Investment to update previous FDI regime. Negative list updated December 2021.

EU Foreign Subsidies Regulation (‘FSR’) 2022

Background

- Intended to combat distortive effects caused by ‘foreign subsidies’ from non-EU governments that grant their recipient an unfair advantage in M&A activity and procurement in the EU.
- 12 January 2023 – Foreign Subsidies Regulation (FSR) enters into force.
- 12 October 2023 – mandatory notification obligation for qualifying M&A transactions starts.

Thresholds

- FSR requires notification of large M&A deals and tenders for public contracts:

➢ **M&A:**

Mandatory notification triggered if:

i. the *target* or a *joint venture* has EU-wide turnover **≥ EUR 500m** in the previous financial year,

AND

i. (ii) the *parties* have received combined *foreign financial contributions* **≥ EUR 50m** in the previous three years.

➢ **Procurement**

Mandatory notification triggered if:

i. (a) the value of the award is **≥ EUR 250m**, OR
(b) if divided into lots, the aggregate value the bidder is bidding on totals **≥ EUR 125m**

AND

i. the ‘bidder’ has received *foreign financial contributions* of **≥ EUR 4m** in the previous three years (this threshold applies per country).

Application

- **‘Financial contribution’:** Very broadly defined to include (e.g.) capital injections, (zero-interest) loans, grants, guarantees, debt forgiveness, tax breaks and the provision or purchase of good or services by public authorities or other public or private entities whose actions can be attributed to a non-EU country.
- **‘Non-EU country’:** Includes contributions provided by, and commercial relationships with central government & public authorities at all levels, plus private and public entities whose actions can be attributed to a third country. This catches government departments and agencies, sovereign wealth funds, and potentially public sector pension funds.

Regulatory Hurdles: Sanctions

Investment: All or certain "new investments" prohibited in Russian Federation.

United States

- Any commitment of capital or other assets for purposes of generating returns or appreciation, including acquisition of equity and debt securities and profit sharing arrangements
- **Targets:** entities incorporated in Russia and individuals ordinarily resident in Russia; may target entities outside Russia if their revenues predominantly come from Russian investments
- U.S. persons are authorized to settle and clear divestment transactions between non-U.S. persons (i.e. possible to use USD

United Kingdom

- Acquire any ownership interest in or control over a person connected with Russia, or any non-Russian legal entity for the benefit of any person connected with Russia, establish any joint venture with a person connected with Russia, provide investment advice for such transactions
- Deal in securities issued after 1 March 2022 and grant loans
- **Targets:** Persons connected with Russia - individuals ordinarily resident or located in Russia, or legal entities incorporated or domiciled in Russia.

European Union

- Acquire any new or extending any existing participation in targeted entities, grant new loans or credits or otherwise provide financing to them, create any new joint ventures with them, or provide investment advice for such transactions
- **Targets:** entities incorporated in Russia or in a third country that operate in energy, mining or quarrying sectors in Russia; entities that own or control an entity operating in the targeted sectors
- Invest or otherwise contribute to projects co-financed by RDIF

Regulatory Hurdles: Impact on Dealmaking

- Heightened Diligence Process
  - Target Operations/Activity – Sanctions/CFIUS
  - Reverse Diligence – Buyer portfolio companies/composition of investing group
  - Sensitivity to Competition Law in Conducting Diligence

- Longer Sign to Close
  - Impact on financing
  - Interim Operating Covenants

- Focus on Regulatory Cooperation Obligations

Any Questions?