

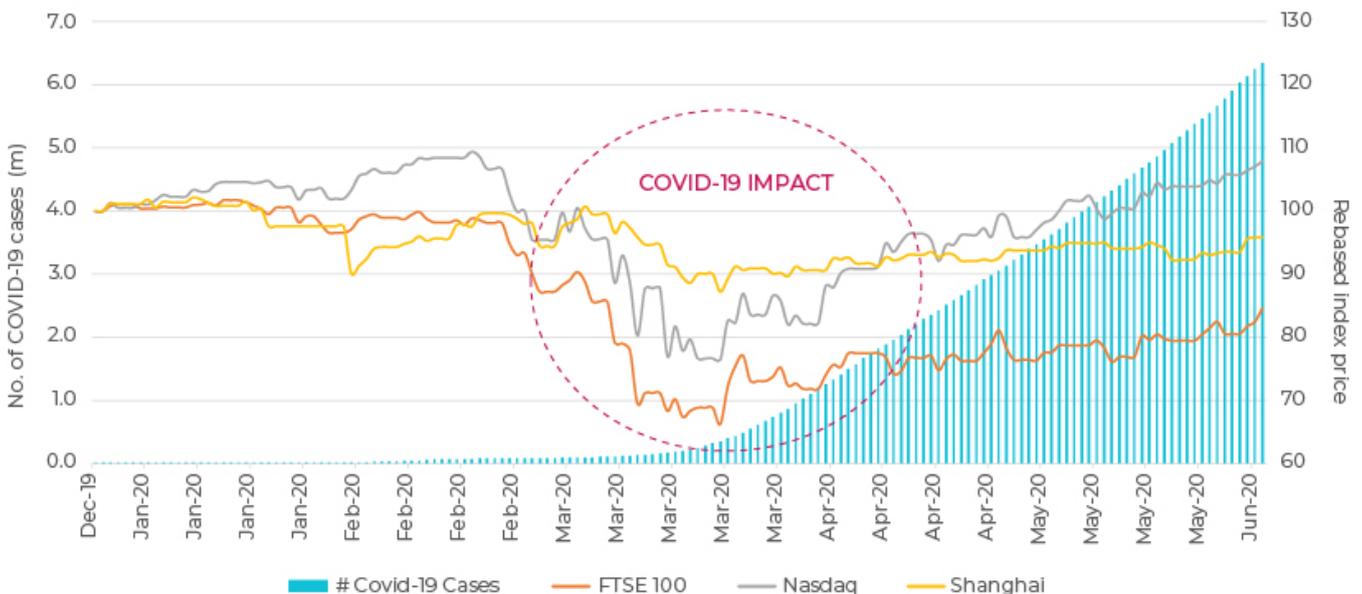
PRIVATE EQUITY GEARING UP FOR THE DISTRESSED MARKET?

Rahul Thakur

As hard as it may be to believe what is happening to the world and although it may feel like the plot of an end-of-the-world Hollywood movie, investors in a particular type of asset class seems to be actually shifting gear when almost everything around us is at a standstill.

We are referring to private equity (PE). My last blog was on PE dry powder accumulating due to increased funding by investors and limited market opportunities for PE firms to invest. PE firms could definitely not have predicted that a crisis such as this would occur, putting the entire world at risk, but in terms of market opportunities, this is the kind of time when PE firms are most active, closely watching for opportunities as company valuations drop, with some sectors worse hit than others.

The following graph shows the spread of the virus compared to the performance of global stock markets



Source: Investing.com, ourworldindata.org/coronavirus

Many PE firms have shut their offices, but deals past the stage of due diligence are still being transacted (as employees work from home), although deals in the early stages have slowed. However, this has **not stopped these firms from preparing for opportunities likely to arise amid the “new normal” course of business.**

Many are ready to grab as many opportunities as they can, including some they may have shelved earlier, for example, because they did not have much traction but have such potential now as the scenarios for some sectors have changed.

Economic uncertainty weighs in

The current market conditions would have a negative effect on PE firms as well, as the valuations of their portfolios are sure to be affected and PE-to-PE transactions would decrease. In addition, their holding periods are likely to be extended, at least for a while, due to the lower portfolio valuations. **New deal activity would all but cease, although preparation for potential opportunities would not.**

Howard Marks (co-founder of Oaktree Capital) quoted recently that **“If you’ve never experienced something before, you can’t say you know how it’s going to turn out”**. The context is you cannot be prepared for something and predict correctly which you have never seen before. We agree, forecasts are based on historical data, and we have not seen a pandemic such as this in the past 100 years.

However, we have seen recessions before, one just almost a decade ago, and we know what happened to PE activity at the time, and currently we believe, that we are not heading into but are already facing a global recession, one that is deepening daily. **Thus, we can expect what is going to be the course of path for PEs, especially for distressed debt investors.**

Dry powder increases through fundraising: PEs gearing up for the market

The cash available on hand due to the pre-crisis scarcity of relevant and right-value deals will come into play now, boosted by new fundraising. Fundraising has also been affected, but large funds of the more established fund managers are securing considerable capital commitments.

According to a recent Preqin report, 267 funds closed in 1Q 2020, marking a 27% drop vs 1Q 2019.

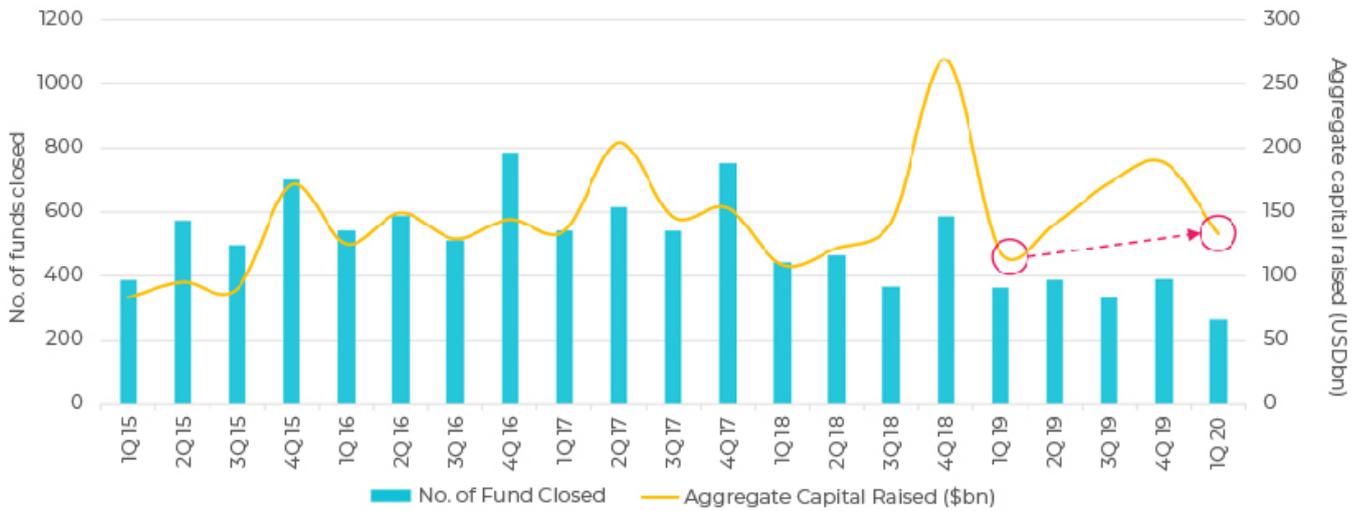
However, a significant amount of capital was raised - USD133bn - almost 12% more than the USD119bn in 1Q 2019. It also reports that large funds of the more established fund managers are securing considerable capital commitments amid the current conditions. Other news relating to fundraising also confirms investors’ and PE firms’ confidence in the market despite the economic uncertainty created by the coronavirus pandemic:

Recent Announcements

COVID-19 infection cases as of 03 June 2020: c.6.3m

- **Oaktree Capital** plans to raise a USD15bn distressed-debt fund (**the biggest to date**) and will buy debt from virus-hit companies
 - **Silver Lake Partners** is also planning to raise a new buyout fund (Silver Lake Partners VI) of about USD16bn in 2Q 2020
 - **Insight Partners** has raised USD9.5bn for its newest and **largest PE fund** (Insight Partners XI)
 - **Clearlake Capital Group**, too, has raised more than USD7bn for its sixth PE fund (Clearlake Capital Partners VI LP)
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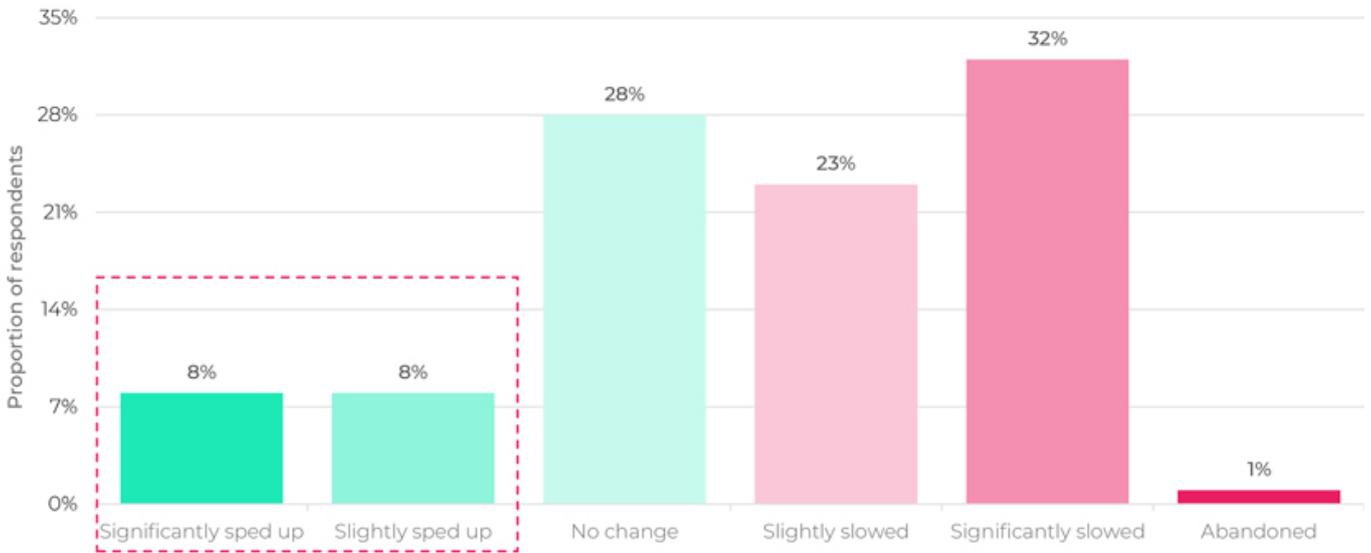
Global quarterly PE fundraising, 1Q 2015 to 1Q 2020



Source: Preqin Quarterly Update, Private Equity and Venture Capital, 1Q 2020

A Preqin survey in April revealed that 55% of the fund managers surveyed had their fundraising processes slowed by COVID-19, with just 1% choosing to abandon their fundraising efforts. **This is notable, but what about the positive side - the remaining 44%? Of these, 16% said their fundraising processes had accelerated, and 28% experienced no change. We believe the net result of this survey is positive.**

Fund managers' views on how COVID-19 has affected their fundraising processes



Source: Preqin Fund Manager Survey, April 2020

The lockdowns, travel restrictions and social distancing are affecting not only our lives, but global industry as well. PE firms have not been spared, **but as the market adapts to the new normal, the effect on such firms' activity may start to diminish**, and a good share of them would be ready to take on the market.

How Acuity Knowledge Partners can help

One of our prominent clients stated that during the 2009 recession, we were its "secret weapon" as our "Super 30" team helped it stay ahead of its peers. We help with target screening, industry studies, company profiles, investment memos and valuation work. We handle all critical work that the client does

not need to keep in-house, and provide an edge in pitching for the right deal at the right time. We have the right experience and talent to provide support in turbulent times. We have done it in the past, and we can do it again!

To help our clients navigate both the people and business impact of COVID-19, we have created a [dedicated hub](#) containing a variety of topics including our latest thinking, thought leadership content and action oriented guides and best practices.

“The spread is moving quickly, and the facts & figures in this blog may fall swiftly out of date. This write-up reflects my perspective as of June 03, 2020.”

Sources:

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<https://www.oaktreecapital.com/insights/howard-marks-memos>

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About Acuity Knowledge Partners

Acuity Knowledge Partners is a leading provider of high-value research, analytics and business intelligence to the financial services sector. The company supports over 300+ financial institutions and consulting companies through a team of over 2,500+ subject matter experts who work as an extension of the clients' teams based out of various global delivery centres.

We empower our clients to drive revenues higher. We innovate using our proprietary technology and automation solutions. We enable our clients to transform their operating model and cost base.