# Private Market Pulse

## September 2023

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## The private equity market: a $7.6-trillion playground[1]

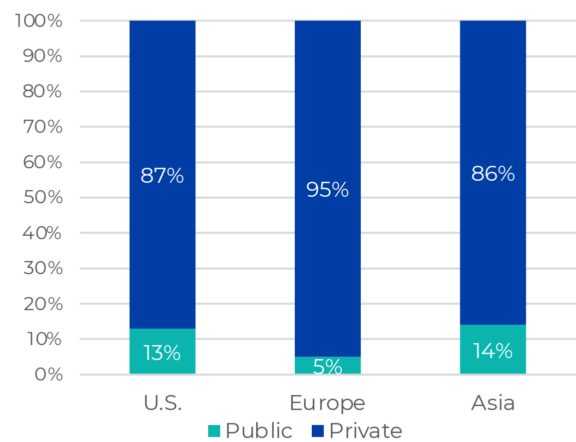
"Private equity is just leveraged buyouts!" Ever heard someone say that? It's probably one of the biggest misconceptions about private markets. The first question to elucidate is "What is a private company?" The answer is simple: a private company is a company whose shares are not offered publicly.

The definition runs the gamut from a small neighbourhood business selling HVAC to residential and industrial customers to a behemoth such as Ikea, a worldwide furniture store with annual sales of more than €39 billion. Thus, the private market includes a large variety of businesses in terms of size, sector and financing structure.

The comparison with the public market speaks for itself. As of February 2022, there were 95,000 private companies in the world with annual revenues exceeding $100 million, whereas the number of equivalent public companies was only 10,000. Not only is the number impressive, but the trend is also revealing. As the number of PE-backed companies in the United States increased from 2,000 in 2000 to 8,000 in 2018, the number of publicly listed companies shrank by more than 60% during the same period.

This playground allows us to build a diversified portfolio with companies in different stages of their business life. Investments in smaller, younger companies benefit from their innovation and growth, a profile found less frequently in the public market, considering the size required to enter it, whereas investments in mature companies that can sustain higher leverage offer stable cash flows for the portfolio. In summary, the private market is a vast, diversified market that needs to be considered in portfolio construction. So, it's not just all leveraged buyouts!

**Public and Private Companies**
LTM Revenue > $100M




Source: Hamilton Lane, Capital IQ, February 2021 – February 2002

### Did you know?

During fundraising, the initial phase of a fund cycle, a private manager reaches out to potential investors and presents the fund's strategy. The objective is to raise money, defined as commitments from limited partners.

Once the final closing occurs, typically after about 18 months, the fund's size is established on the basis of the total commitments received. The private manager then has a mandate to invest all commitments progressively through capital calls during the investment period, which is typically five years.

1. Source: McKenzie. The size of the entire private market (including infrastructure, real estate and private debt) is estimated at $11.7 trillion according to the same source.

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## Market Highlights

- Fundraising is slowing because institutional investors (LPs) have capital constraints, mainly for two reasons. The first is the denominator effect, which has a reduced impact as a result of the stock market's rally in the first half of 2023. The second is the challenging M&A and public exit environment, which has had a significant impact on funds' distribution pacing; many LPs must deal with negative cash flows that limit their ability to participate in new fundraising. During the first half of the year, $517 billion was raised, a decline of 35% from 2022.
- This turn of events has put increasing pressure on private managers to generate distributions, which has led to a new market expression: "DPI is the new IRR." [1] We expect that finding a way to return capital to LPs will be a general focus for general partners (GPs) in the coming months.
- Private market dry powder remains at an all-time high of $3.7 trillion ($1.1 trillion for buyouts[2]). Considering that the vast majority was raised over the past three years, GPs still have the flexibility to wait patiently for a better market environment.
- The number of buyouts has declined since the first interest rate increase in mid-2022, falling 29% on a year-on-year basis. Of the deals closed, 56% were add-ons,[3] which are often easier to finance internally owing to their smaller ticket size. Deal value has dropped more significantly, indicating that the vast majority of activities remain in the middle market.[4]
- The asset manager consolidation trend remains active, with 39 deals already done as of July, for a total of $13 billion, which is already $2.6 billion more than the peak reached for the whole of 2021 ($10.4 billion). Asset managers are moving away from a unique strategy toward a multistrategy approach to reinforce relations with LPs through multiple offerings.
- In case you missed it, Blackstone became the first private equity firm to reach $1 trillion in AUM.

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1. DPI refers to "distribution to paid-in" and IRR to "internal rate of return."

2. Traditionally, a buyout is a majority investment in a mature company with the intend to restructure its finances, governance and operations to maximize returns.

3. Refers to the purchase of a smaller-sized target by an existing portfolio company, where the acquired company is integrated into the existing portfolio company.

4. Middle-market businesses are generally defined as having revenues from $10 million to $1 billion.