HITTING NEW HIGHS

December 2021

Overview

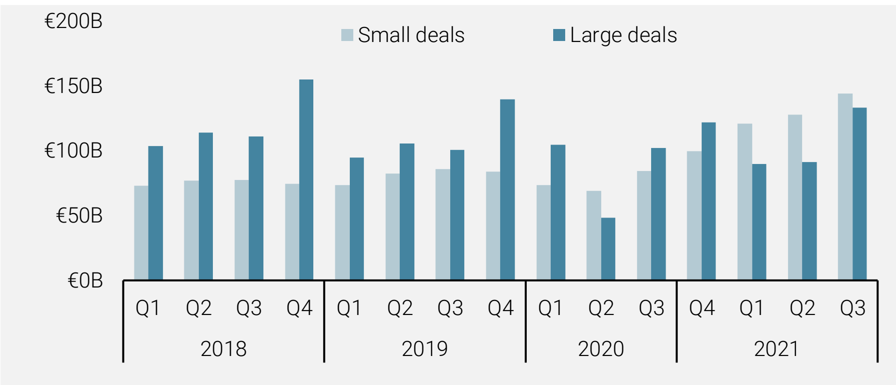
Private equity investment activity continued to reach record highs in Q3 2021, with a 49% increase on a predictably depressed Q3 2020. However, even compared to pre-COVID times, the first three quarters of 2021 were still 30% higher versus the same period in 2019. Private equity investors continue to be buoyed by strong growth fundamentals, cheap debt and supportive limited partners keen to see their money work. Meanwhile, exit activity is rejuvenating but was only up 10% in Q3 versus the same quarter a year ago. For the year to date, exit activity is now back to pre-COVID levels, on a par with the same period in 2019. This suggests that exits have on average simply been delayed by 12 months due to the COVID pandemic and investors' capital is therefore being tied up for longer periods.

Robust Investment Activity

The global aggregate value of private equity deals closed in Q3 2021 was EUR 277bn (+49% vs. Q3 2020)1. Activity was strong in all regions with North America posting the highest increase, given that the fall in this region had been most dramatic in the first half of 2020.

Following the trend of the last few quarters, investment activity in small and mid-market companies (defined as deals with an enterprise value of less than EUR 500m) continues to lead the charge. The aggregate value of small and mid-market deals increased by 80% in the first three quarters of 2021, compared to 40% for large deals. Only in North America did the growth of large deals (87%) exceed that of small and mid-market deals (79%), whereas in APAC the investment activity at the large end even declined slightly (-4%) compared to the same period last year.

Figure 1: Investment Activity by Deal Size (EUR bn)



Source: Pitchbook. Data as at October 2021.

Paul Newsome

Head of Portfolio Management, Private Equity

Key Points

1. Following the trend of recent quarters, small and mid-market deals were the main drivers of investment activity in Q3.
2. Private equity investors continue to be buoyed by strong growth fundamentals, cheap debt and supportive limited partners keen to see their money work.
3. YTD, we committed EUR 449m to investments, including EUR 111m invested in 14 secondary transactions and EUR 161m invested in 9 direct co-investments.

[1] Pitchbook, October 2021.

So far in 2021, the Unigestion Direct II strategy has made 10 investments, taking the portfolio to 16 in total. While we are seeing more deals than ever, we have remained disciplined and have been able to invest in high quality, high growth companies playing our key investment themes at attractive valuations.

In July 2021, we led a growth capital investment in Singapore-based Ascenda Loyalty. Having known the company for several years, we sourced this opportunity directly. Ascenda provides full end-to-end credit card loyalty services for global financial services firms. We were particularly attracted by the company's tier-one customer base, its attractive recurring revenue profile with 5-year contracts as typical and increasing spend of existing customers, and the high visibility of future growth through its continued penetration of both established and "neo" banks.

In September, we led a direct investment in Switzerland-based Home Instead, a leading provider of non-medical care services to the elderly at home. Driven by an ageing population, increasing desire for at-home independence and regulatory tailwinds, the non-medical home care market is growing at 7 – 9% p.a. In addition, we are backing a highly incentivised management team, where the founder remains a significant owner in the business. Finally, there are tangible growth opportunities for the company, including a pipeline of over 40 potential add-on acquisitions.

Private equity exit activity has been steadily growing, albeit not matching the pace of investment activity. The global aggregate value of exits in Q3 2021 was EUR 192bn, 10% up on the same quarter last year. There was quite some regional variation. On one hand, North America was flat while, on the other hand, Europe (+30%) and APAC (+102%) saw material growth. Overall, 2021 exit activity is now clearly back to pre-COVID (i.e. 2019) levels.

As discussed previously, 2021 marks the year where GP-led secondary transactions have clearly become the fourth 'exit' option for GPs after IPOs, trade sales and sales to other financial sponsors. With the support of secondary investors, such transactions give GPs the ability to continue owning their best performing assets while giving existing LPs the option to take liquidity.

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After the onset of the COVID pandemic, the dearth of liquidity was the catalyst for the rapid increase in GP-led transactions. Today, even with exit activity back to its pre-COVID levels, both GPs and LPs like the optionality that such transactions permit. This explains why, in 2021, it is expected that GP-led transactions will account for around 57% of the secondary market, which is on track for its biggest year ever.

Nevertheless, while our strategy of targeting concentrated portfolios of high quality companies lends itself very well to tailored GP-led transactions (so far in 2021, 8 of our 12 secondary transactions completed were GP-led), we are also seeing attractive secondary opportunities in acquisitions of LP stakes in funds we know well and structured deals such as sidecars investing alongside mature portfolios.

In September, we purchased a single LP interest in Euroknights VII, a maturing portfolio of 14 companies. As an existing investor in this fund through our other programmes, we know the portfolio well. There is strong visibility on early liquidity with attractive upside potential: three of the companies are exiting in the coming few months, while three others will soon deliver partial liquidity. Furthermore, the portfolio companies are attractively valued (8x EBITDA on average), are showing robust current trading activity (over 15% annualised growth) and have low leverage (less than 3x EBITDA).

Our latest secondary strategy, Unigestion Secondary V, is now over 50% committed to 20 transactions (including those in closing). At Q2 2021, the strategy is valued at close to 1.5x, driven by strong growth in the underlying portfolio companies. For example, the first five deals, which were completed between September 2020 and February 2021, are already showing between 20% and 120% EBITDA annualised growth since we invested. With over EUR 500m raised to date, the final close of this strategy will be held on 31 December 2021.

SFDR in a Nutshell

ESG has become a key topic over the last decade. Not only is it at the centre of our personal lives but it has also become a major point of focus for the financial and asset management industries. However, for many investors, ESG has become a buzz term which has been increasingly thrown around without material substance or standardisation.

At Unigestion, ESG has been integrated into our due diligence process for over 10 years. Not only do we view this as a key way to identify and mitigate certain risks, it is also central to our strategy of investing in sustainable business models. Furthermore, with the appropriate measurement and engagement on certain ESG criteria, we can share best practices with portfolio companies and fund managers to enhance their ESG standards. This leads to both better financial returns and better outcomes for society.

"We share best practices with portfolio companies and fund managers to enhance ESG standards, leading to better financial returns and better outcomes for society."

However, in order to bring all financial firms up to a minimum level of ESG integration, as of March of this year, the EU has introduced a new package of regulations, the Sustainable Finance Disclosure Regulation (SFDR). Its objective is to ensure that financial market participants (in our case, private equity firms) are able to finance growth in a sustainable manner over the long term while combating 'greenwashing'.

A key part of these regulations is also to promote transparency, requiring firms to explain how they: (i) integrate E, S and G into their investment decision--making process and manage their ESG-related risks, (ii) take into account the adverse impacts of their investments on sustainability, and (iii) justify any investments, products or services labelled as 'sustainable'.

In the concrete case of a private equity firm either based in the EU or marketing to EU investors, the SFDR is applied through the adherence to various Articles including:

- Articles 3 & 5: Integration of ESG risks in the investment and remuneration policies of a firm.
- Article 6: Assessment and consideration of ESG risks when making investments. These risks must be monitored and reported to investors at the fund level.
- Articles 4 & 7: Evaluation, measurement and reporting of adverse impacts on investments. There are at least 14 KPIs, such as a company's carbon footprint and board gender diversity, known as the Principal Adverse Impact (PAIs) indicators, which need to be used. Article 4 is applicable to private equity firms from 2022 and Article 7 is applicable to private equity funds from 2023.
- Article 8: Positive impact on at least one environmental and / or social goal. UN Sustainable Development Goals (SDGs) are an example of goals that can be targeted under this article or Article 9 (see below). This is applicable to funds.
- Article 9: Positive impact on at least one environmental and / or social goal, Do No Significant Harm (DNSH) assessment and evidence of good governance. This is also applicable to funds and allows compliant investments in the fund to be labelled as 'sustainable'.

Currently, it is mandatory for private equity firms to adopt Articles 3, 5 and 6 while the others are optional.

The best way to illustrate the application of these Articles is through an example. Our current direct strategy, Unigestion Direct II, has been compliant with Article 8, as well as Article 6, since March 2021.

In May 2021, on behalf of Unigestion Direct II, we invested in LMG, a US company which provides alcohol monitoring devices and services for people who have been convicted of Driving Under Influence (DUI) offences. Using these devices, in lieu of prison, offenders are continuously monitored to prevent reoffending.

When we began our investment review, the first step was to confirm that, in compliance with Article 8, the main economic activity of the company makes a clear and measurable positive contribution to at least one of the SDGs. Indeed, LMG's products and services contribute to SDG 16 – Peace, Justice & Strong Institutions – by reducing re-offending, jail sentences, and the risk of alcohol offenders harming society through drunk driving or otherwise.

We then ran our usual ESG process. Firstly, we confirmed that the company did not breach our exclusion list aligned with UN PRI. Secondly, we checked against three key ESG negative indicators: (i) Does the company not have, or not intend to have, an ESG policy in place? (ii) Has the company faced major ESG-related litigations in recent years? (iii) Is the company identified as a high carbon emitter (assessed quantitatively or qualitatively)? An answer of yes to any of these indicators would be an immediate deal-breaker.

In accordance with Article 6, we made a qualitative and quantitative assessment of the key ESG risks that could materialise during our holding of LMG. The Sustainability Accounting Standards Board (SASB), of which Unigestion is a member, is an important tool to support our pre-investment assessment and post-investment monitoring.

We then ran two stress case scenarios to understand the financial impact based on relevant ESG risks: (i) the ESG case, based on the material ESG risks identified in the company and (ii) the climate change case, based on chronic climate-related risks (i.e. global warming). For LMG, we looked at the impact of its complex supply chain, most of which is offshore, on the environment. In financial terms, the greater the environmental impact, the greater the risk that costs will rise through, for example, the application of carbon taxes. However, for LMG, the environmental impact of its devices is small since they are light (less than 200g) and have a 5 to 10-year life.

Finally, we rated the company on our ESG scorecard. A low score does not preclude an investment but will highlight areas for improvement which can be achieved through engagement with the company under our ownership. In the case of LMG, it had a score of 12.8 out of 20, making it an ESG "follower". The company was strong in most areas, apart from the tracking of its environmental impact. Therefore, we and our investment partner, Riverside, have started engaging with the company to install best practices around, amongst other things, carbon footprint measuring.

Importantly, in our quarterly reporting for Unigestion Direct II (and soon for all of our strategies), we now report on the positive contribution to SDGs (Article 8) and the ESG score of each portfolio company.

Given our 10-year journey of ESG integration at Unigestion, the latest additional regulatory requirements fit very well within our overall process. Overall, the regulations will help investors gain comfort that ESG criteria are being applied, measured and enhanced in a transparent and standardised way across the portfolio companies and funds within all of our various investment programmes.

Unigestion Direct II and Unigestion Direct II Diversification Européene are our first Article 8 compliant strategies. We will soon launch our first Article 9 compliant strategy – Unigestion Climate Impact strategy – but more on that to come.

"The new regulations will give investors confidence that ESG criteria are being applied, measured and enhanced in a transparent and standardised way across the portfolio companies and funds."

Unigestion Private Equity Activity

In the first nine months of 2021, the Unigestion private equity team committed EUR 449m to investments. We have closed six new primary funds of EUR 84m. In addition, we completed 14 secondary transactions totalling EUR 204m, and closed nine direct co-investments of EUR 161m in total. Here are the highlights of some if the investments and exits that we completed in Q3:

Loyal Valley Capital

In July, Unigestion committed to Loyal Valley III. Loyal Valley is a Chinese private equity firm founded in 2015. It pursues a research-based thematic investment strategy in fast growing and resilient sectors driven by long-term secular trends in China and low cyclicality industries. The firm's three core themes are consumption driven by the young generation, healthcare driven by an aging population and industrial transformation driven by import substitution and 5G roll-outs. Loyal Valley is known for successfully driving value creation initiatives.

UFENAU CAPITAL PARTNERS

Also in July, Ufenau V, one of the Swiss funds in our primary programmes, exited Swiss IT Security Group (www.sits-group.ch), generating proceeds of EUR 4.7m. The company is a leading cyber security services provider in its core markets, providing strategic cyber security consulting and implementation support, managed security services and software solutions. With 19 offices in the DACH-region and Benelux, the company is active across all business sectors, serving corporations, SMEs and public institutions by protecting their IT infrastructure and combating cybercrime. The transaction resulted in a gross TVPI of 12.0x and 150% gross IRR.

Coastal Waste & Recycling

In August, Unigestion invested in a single asset continuation fund to acquire Coastal Waste & Recycling (www.coastalwasteinc.com), a rapidly growing solid waste hauling and processing company in southern Florida. Florida is the second fastest growing state in the US (14% population growth from 2010-2019) underpinned by post-COVID demographic trends, warmer weather and lower tax rates.

The company is managed by Summer Street Capital, an experienced investment manager with a demonstrated track record in the solid waste sector having successfully built and exited six regional platforms across multiple geographies. Over the investment period, the management team will continue to drive strategic growth through densifying the operating footprint in the company's core markets and expanding into adjacent markets. Furthermore, it will continue the expansion of vertical integration and pursue additional municipal/franchise opportunities.

Adista

In August, Unigestion closed a direct investment in Adista (www.adista.fr). Adista is a French value-added B2B ICT operator providing connectivity, telephony and unified communications, as well as IT services to SMEs (including public authorities, healthcare and retail companies) in France and internationally. Its direct proximity-based business model is powered by 35 local agencies.

Adista's addressable market is expected to grow at 7% in the next five years as the result of increases in digitalisation, unified connectivity and IT needs of SMEs. With the company being able to offer the full range of services covering both segments, IT and communications, and bundled into unified and tailored solutions supporting the convergence of IT and connectivity services, the company should be able to deliver above market organic growth.

CAFPI EXPERT EN CRÉDITS

In the same month, Unigestion closed a direct investment in CAFPI (www.cafpi.fr). Founded in 1971, CAFPI is a leading mortgage brokerage company based in France with 230 agencies, over 1,000 independent advisors and 150 partnerships with banks and insurance companies. The company has the second largest brokerage network in France and a strong brand, recognised by consumers for its expertise and quality of service.

With the French retail mortgage production steadily growing at 13% year-on-year over the last decade and CAFPI having a market share of roughly 10%, there is a strong growth opportunity in combination with the company's ambition to improve digitisation to generate more leads online and gain in efficiency.

Also in August, Unigestion committed to MED III. MED III is managed by Archimed, a healthcare-focused GP investing in European and North American profitable and growing healthcare companies with a view to professionalise and internationalise the business. The growth strategy, with typically no or only limited leverage at entry, is focused on six core sub-sectors: Medtech, BioPharma, Life Science, Healthcare IT, Diagnostics and Consumer Health. Within these sub-sectors, Archimed goes one level deeper to focus on the more promising sub-sub-sector, making it the most specialised healthcare-focused GP in Europe.

In September, Xenon VI, one of the Italian funds in our primary programmes, exited ReLife (www.relifegroup.com). ReLife is a fully circular waste management and recycling company. It specialises in the collection and treatment of paper, plastic and ferrous material waste to produce, amongst other things, cardboard and cardboard packaging for industrial use as well as secondary solid fuel, used in industrial production processes to replace fossil fuel. The transaction resulted in a gross TVPI of 4.7x and 71% gross IRR.

Also in September, Accent 2012, one of the Nordic funds in our primary programmes, exited two companies generating gross proceeds of EUR 4.8m. One company is Cervera (www.cervera.se), a Swedish retailer of kitchenware. The transaction resulted in a gross TVPI of 3.5x and 15% gross IRR. The other company is Brenderup (www.brenderup.com), Scandinavia's largest provider of car trailers. The transaction resulted in a gross TVPI of 8.8x and 44% gross IRR.

In the same month, Polaris IV, one of the Nordic funds in a mandate account, exited ProData (www.prodataconsult.com), generating gross proceeds of EUR 1.8m. ProData is a leading provider of high-end IT consultants, both through its large network of local freelance consultants and its Nearshoring-as-a-Service offering. The transaction resulted in a gross TVPI of 5.3x and 95% gross IRR.

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