INSIGHTS

JANUARY 2025

GLOBAL OUTLOOK 2025

FOREWORD

Could 2025 be a year of exits? Many of the world's top managers think so, as the M&A machinery eases back into action. The FT reports that the US IPO market is set to rally – fuelled in large part by anticipated policy shifts – creating a much-needed outlet for the global asset logjam in private equity (PE).

A record-breaking secondary market is also greasing the deal wheels – the pressing need for liquidity has dispersed much of the stigma that surrounded the space, with heightened awareness and sophistication in the GP-led segment powering unprecedented growth. Most of the contributors to this report highlight this as a rich vein in the market.

Still, as we anticipate a healthier deal landscape, challenges of the past few years have left their legacy.

More managers are focused on tangible, operation-based value creation strategies. A rising number of high-opportunity niches are emerging – the middle market being one, much-cited example. And the astronomical growth of credit as an asset class continues, as an expanding pool of capital stratifies into new tranches and sub-segments across portfolios.

Underpinning all these developments, private markets continue to be an effective force for change – as investors and asset managers align themselves with global megatrends such as digitalisation, ageing populations, supply-chain redevelopment, the energy transition, and many others.

We're certainly excited to map the ongoing evolution of the industry, and would welcome as many insider perspectives as possible to help us on this journey. For now, here are some of the biggest names in PE, generously giving us their view on where we are, and what we stand to gain in 2025.

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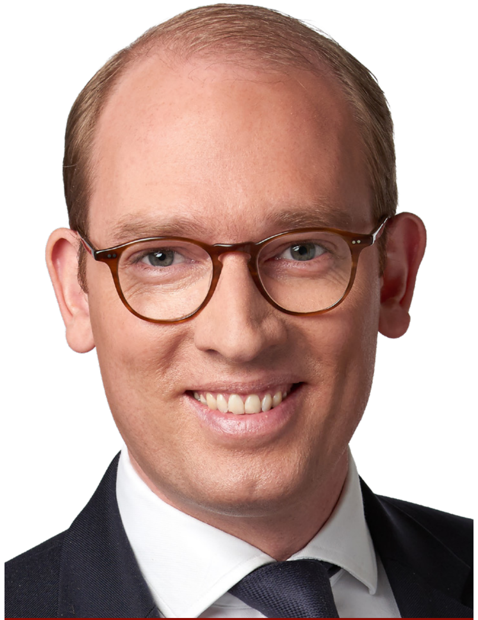
MARKET OVERVIEW

How some of the world's leading asset managers and allocators perceive the scope for growth in private markets in 2025 and beyond



ALBRECHT VON ALVENSLEBEN
MANAGING DIRECTOR,
PRIVATE EQUITY EUROPE

CDPQ

2024 marked a mixed yet improving landscape for European PE. We expected a challenging market following the disruption of previous years, but now see improved momentum – especially for cycle-tested investors like CDPQ – to access unique opportunities as we head into 2025.

The start of the year was marked by limited activity in private markets as high interest rates, inflation, and valuation gaps continued to hamper dealmaking. In line with the broader market, we used this period to focus on enhancing operating performance and cash flow generation in our portfolio, ensuring we were set up for success when conditions improved.

Through the summer months, we saw increasing activity in private markets, driven by an easing of monetary policy across the Eurozone and UK, which helped drive investor confidence. In particular, assets in the technology, healthcare, and sustainability-driven sectors attracted interest. We were able to capitalise on this dynamic via the divestment of Techem, a leading provider of energy efficiency services to the building ecosystem, and an investment in Aareon, a European SaaS provider for the property industry, alongside our partner TPG.

Despite an uncertain macroeconomic and geopolitical outlook, we anticipate the uptick in deal activity to continue – and perhaps improve – in 2025. The combination of significant accumulated dry powder, constructive debt markets, and optimism around the IPO market is pointing to next year 'unlocking' a backlog of asset sales and deployment. This is further supported by the increasing pressure on GPs to deliver DPI in an environment of increasing average hold periods, which we believe will provide for exciting investment opportunities.

Our focus in the year ahead will be to position ourselves on a select number of resilient assets in the software, healthcare, business services and financial services sectors that are supported by secular growth trends – which has proven to be a winning strategy for us across cycles, and with which we have built a strong track record.

As a minority investor with direct investment teams and operating partners on the ground across North America, Europe and the APAC region, we expect 2025 to offer attractive opportunities for us to act as facilitator to unlock transactions on the one hand, and as a value-add partner for our GPs and target businesses on the other. ■

In 2025, we anticipate substantial growth in investment opportunities in the industrials sector, supported by industrial macro tailwinds, a favourable deal environment and a robust pipeline of opportunities. Falling interest rates – albeit not close to historical lows – and a strong debt financing market indicate that PE firms are likely to encounter healthier conditions for dealmaking than they have for several years.

TREND MAPPING

Several macroeconomic and industry-specific factors underpin our positive outlook.

In terms of larger trends, US power demand is projected to grow for the first time in years, with some pointing to a compound annual growth rate (CAGR) of 3% across residential, commercial, industrial, and transportation sectors. This expected return to growth is partially driven by the steady construction of new data centres – a trend fuelled, in turn, by the rise of artificial intelligence. The movement presents significant opportunities, not only for data centres themselves, but also for ancillary businesses such as testing equipment, maintenance providers and aftermarket parts.

Equally, the industrials sector is likely to benefit from the ongoing shift by manufacturers towards onshoring and nearshoring in the US.

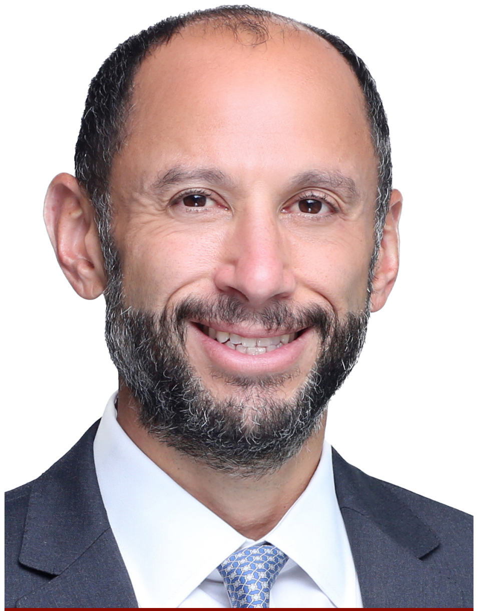
This is a trend that started to gain momentum during the Covid pandemic and has been further accelerated by the prospect of tariffs on international trade, as well as factors such as rising transportation costs, a reduction in lead times and consumer demand for locally sourced goods. These have all combined to incentivise American manufacturers to increase local production rather than rely on previously low-cost overseas markets.

Although bringing production back to the US is a complex and long-term project – new facilities require extensive design, planning, permitting, and construction – we believe there will be growth in 2025 as efforts kick into higher gear. We can clearly see this propensity within our own portfolio. Vibrantz Technologies, for example, which produces colourants and additives for a range of end markets, including electronics, automotive and construction, is building a new plant in Mexico to support new technology it is developing. Sub-sectors within the industrials space have their own specific growth drivers. Take agricultural chemicals, an industry that has faced a protracted down cycle stemming from inflationary pressures and a resulting drop in demand.

As a result of these challenges, we are starting to see larger chemical companies selling off non-core assets and businesses to concentrate on core markets such as corn and soybean. This repositioning creates attractive opportunities for investors who have expertise and experience with chemicals, particularly in areas that have become too niche for the largest players.

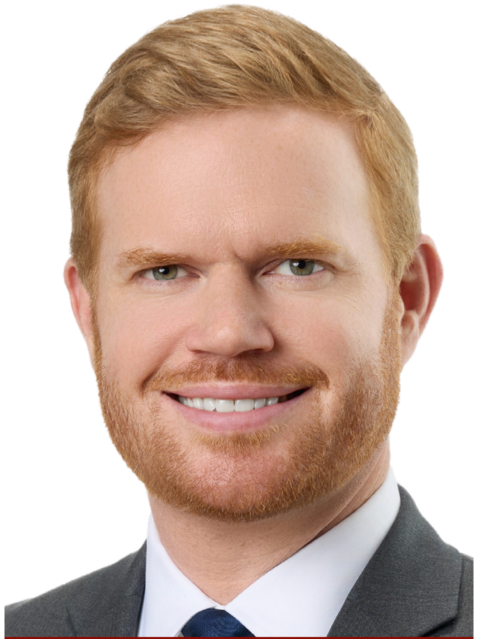
In light of the anticipated growth in mergers and acquisitions activity, our industrials team is taking a highly selective approach, prioritising those businesses where we think we have a unique investment angle and can maximise the likelihood of success. This applies not only to platform acquisitions, but also for add-ons in our core focus areas such as specialty chemicals, building products, and power and energy transition as well as niche industrial manufacturing businesses.

In short, the confluence of macroeconomic trends and sector-specific growth drivers suggests that 2025 will be a busy year for industrials. ■



SCOTT WOLFF
PRESIDENT & MANAGING DIRECTOR

AMERICAN SECURITIES



BROOKS HARRINGTON
CHIEF INVESTMENT OFFICER

FEDERATED HERMES PRIVATE EQUITY

The PE industry is heading into the new year against a healthier economic backdrop, with the US driving global growth forward. Inflation is no longer the problem it was 12-24 months ago, and the Federal Reserve has already begun cutting rates. PE activity has followed suit with improving volumes across deal flow, credit availability, and exit activity. The uncertainty around the US election is over with a major stock market rally on Trump's first day as president elect – a promising sign.

PE is now a mature asset class and investors need to be disciplined in their capital deployment in 2025 in order to continue generating expected returns. In 2024, valuations and leverage appeared to have plateaued from their post-2021 peaks and revenue multiples have come down amid a focus on profitability and capital-efficient growth. The 'democratisation' of PE will continue to gather momentum as the wealth and retail market offers the industry the largest opportunity for raising new capital.

FOCUS ON RETURNS

Liquidity remains constrained with exit activity at multi-year lows. The industry appears more optimistic for 2025, and there is a growing sense that activity is now picking up, with volumes rising and spreads narrowing. The PE industry has undergone a perhaps irreversible mindset shift with regards to returns. For many years, the internal rate of return (IRR) was the industry's default measure of performance and sufficient in a world where cash was cheap and exit routes were generally open. In recent years, the persistent disconnect between buyers and sellers means that a portfolio's paper value may not come to fruition.

This year, we have seen that when LPs are evaluating performance, they increasingly want to know whether these assets can be realised at their current valuation. Many LPs are therefore no longer willing to accept the highest IRR as the sole measure of a fund's success. The DPI ratio – which measures actual cash returns relative to the invested capital – will continue to become an increasingly significant metric for investors over the next 12 months.

AREAS OF OPPORTUNITY

The lower mid-market continues to be an exciting area that is less efficient, crowded and intermediated, with significant opportunity for operational value add – to move the needle and help companies reach scale and reward investors with outsized investment returns.

We expect to see an active add-on market in Europe, as longer hold periods create opportunities for GPs to introduce mid-cycle co-investment opportunities. Buy-and-build strategies are expected to be a popular value driver in the persistently challenging organic growth environment. Further, we are seeing a number of high quality 'stranded' assets in the public markets, particularly those smaller businesses that struggle to attract attention from equities investors. We therefore expect to see rising interest from sponsors, with take-private opportunities accounting for a greater proportion of capital deployment in 2025.

HOT SECTORS

AI dominated the conversation in 2024, and with PE barely scratching the surface this year, that trend will most likely continue, although it's true impact continues to be debated. Regardless, technology and innovation will continue to present some of the most attractive investment opportunities across the US.

Europe will continue to lead on addressing climate change, presenting a significant investment opportunity backed up by regulatory tailwinds, government support and institutional appetite. Cross border investment in China remains muted due to geopolitical uncertainty and as a result, other markets in Asia will benefit as a portion of that capital will flow to India, Japan, and Southeast Asia. ■

In 2024, roughly half of the world's population voted in national elections, and in many instances, policy makers were elected with a mandate for change. As these officials take office and implement their various agendas, we believe 2025 will prove to be a year of significant uncertainty and volatility.

At Brightstar Capital Partners, we are long-term investors in the middle market, and we believe the current environment will offer significant opportunities for those who can separate the signal from the noise.

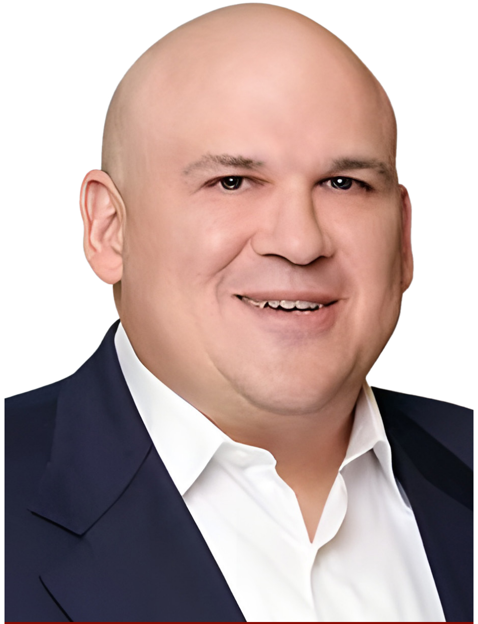
Within our target range for investments, we see three major tailwinds heading into 2025. First, middle market businesses historically have done well in volatile times – a trend we anticipate will continue. It's rarely publicised, but middle market companies created over 2 million jobs in the US during 2007 - 2010, while large businesses shed nearly 4 millionjobs, according to a 2011 report by GE Capital and Fisher College of Business. A combination of smaller size, shorter paths to decisions and closer proximity to their customers can enable middle market businesses to be nimble – and in the case of family-owned businesses, deep pockets and a long-term view can position them to grow through acquisitions when competitors struggle.

Second, the generational wealth transfer will continue its inevitable ascent. Knight Frank forecasts that nearly $90tn in wealth will change hands in the US alone over the next two decades, with a similar dynamic taking place globally. Yet, in Brightstar's most recent "Pulse of Family Business" research, 57% of business owners are unsure if the next generation will join the business, and just over one third say the next generation is ready. We believe these dynamics will facilitate a strong pipeline of quality family businesses looking for a partner.

Third, increased volatility can lead middle market business owners to proactively pursue partners with extensive operational experience. Whether it is reconfiguring supply chains in the face of potential tariffs, stress-testing trade routes in the face of geopolitical uncertainty or assessing the potential impact of AI on the business, it can be difficult for middle market businesses to muster the resources to turn these challenges into opportunities. Every day, our team speaks to founders, families, and entrepreneurs who understand this dynamic, and are excited by the potential of partnering with PE firms that have playbooks and processes in place. The market statistics bear this out – during 2008-2010, US middle market deals accounted for an average of 65% of all buyouts by value, compared to an average of 60% in the years following to 2019. Again, during the peak of the Covid pandemic, middle market deals' share of all US buyout value rose to 64%, compared to an average of 54% in the four years following according to Pitchbook.

We are particularly excited about the lower middle market, where companies show revenues of below $100m. Those businesses historically have under-invested in technology, and new capital can supercharge their readiness for AI and digitalisation, allowing them to realise their full potential at an accelerated pace.

In 2025, we look forward to a year of opportunity for PE firms with a long-term outlook and deep operational expertise, and a particularly exciting year for the partnership between PE and middle market businesses. ■



ANDREW WEINBERG
FOUNDER & CEO

BRIGHTSTAR CAPITAL PARTNERS

NILS RODE
CHIEF INVESTMENT OFFICER

SCHRODERS CAPITAL

2025 presents a promising landscape for private market investments, with favourable cycle alignments offering return and income potential.

Amid geopolitical tensions, private markets are key for portfolio resilience, and despite political changes, we foresee the trend towards decarbonisation continuing with private markets playing a pivotal role.

Buyout valuations have declined in the past three years while stock markets have seen strong rallies, in some cases reaching record highs in 2024. Taken together, this enhances the relative attractiveness of private equity investments. Meanwhile, a correction in fundraising has been most pronounced for venture capital and small to mid-sized buyouts, making these segments particularly appealing for new investments.

Small and mid-market buyouts benefit from direct sourcing from founders and families, and entry multiples that remain more than four times EBITDA below large buyouts. Additionally, the small and mid-market represents a more than 10 times larger investment universe than large buyouts. This brings more opportunities to capture a 'complexity premium', which refers to the potential to capture higher returns by using manager skill to execute on complex and nuanced investment theses.

Venture capital has undergone a healthy correction in fundraising, following the exuberance observed during the pandemic. On the other hand, deal opportunities are being driven by the rise of artificial intelligence (AI), with the share of venture investments in this sector rising from 2% in 2022 to an estimated 15% in 2024. We find early-stage AI opportunities particularly attractive, as valuations for later-stage rounds have increased significantly in 2024 and are now just 20% below their 2021 peak.

Continuation funds present a compelling opportunity for accessing private equity, due to low competition from other exit opportunities and high demand for liquidity from investors as distributions remain below historic averages.

Once a smaller segment of the secondaries market, continuation funds – also known as GP-led secondaries – now comprise around half of the annual market volume. We expect this strong growth to persist as more fund managers leverage continuation funds to extend hold periods and provide new capital to support high-quality companies, while providing valuable liquidity solutions to existing investors.

In an increasingly volatile economic and geopolitical landscape, private markets demonstrate unique resilience due to their structural and strategic characteristics, differentiated risk premia and long-term considerations. These assets offer a buffer against public market fluctuations, providing stability amid potential market shocks.

Moreover, thanks to concentrated investments in sectors underrepresented in public markets, such as, for example, healthcare, renewable infrastructure, disruptive technology and microfinance, private markets offer differentiated exposures that provide positive portfolio diversification. This sector mix enables investors to capture uncorrelated growth, further insulating against cyclical risks.

PE shone during crises of the last 25 years, and has delivered twice the outperformance in challenging conditions. Among other things, this resilience arises from a different industry sector mix compared to public equities, and long-term capital structures that allow fund managers to hold investments and continue to deploy through market disruptions. Crucially, unlike public equities, PE avoids daily price fluctuations, offering more stable valuations based on asset fundamentals. ■

As we enter 2025, the PE landscape presents a mix of opportunities and challenges, shaped by macroeconomic conditions, sector-specific dynamics and geopolitical developments.

A ROBUST ENVIRONMENT FOR M&A

At Tikehau Capital, we anticipate a strong year for M&A activity within PE, supported by several converging factors. Many funds are holding significant levels of undeployed capital, or dry powder, creating a substantial reservoir of liquidity for acquisitions. At the same time, record levels of portfolio assets require monetisation to provide distributions to LPs. Combined with a more favourable macroeconomic environment, characterised by decreasing interest rates and stable inflation expectations, the conditions for deal making are robust. Adding to this positive outlook is the relative stabilisation of the geopolitical landscape following the US presidential election and a reduction in global uncertainty.

STRATEGIC GROWTH SECTORS

Certain sectors in Europe stand out as particularly promising for PE investment, reflecting strategic priorities outlined in the Draghi Report. Decarbonisation and the energy transition remain high on the agenda, with opportunities to improve energy availability and efficiency across the continent. Investments in renewable energy, storage and related technologies are expected to attract significant capital as Europe intensifies its efforts to meet sustainability goals. Similarly, the defence sector is poised for growth, driven by higher defence budgets in major European nations. Even in a scenario where conflicts in Ukraine and the Middle East come to an end, increased demand for advanced defence technologies and aerospace solutions will sustain activity in this sector. Meanwhile, the technology sector is expected to experience significant inflows as Europe works to close the technology gap with the US and China. Investments in areas such as artificial intelligence, automation, and digital infrastructure promise to enhance productivity and competitiveness across the region.

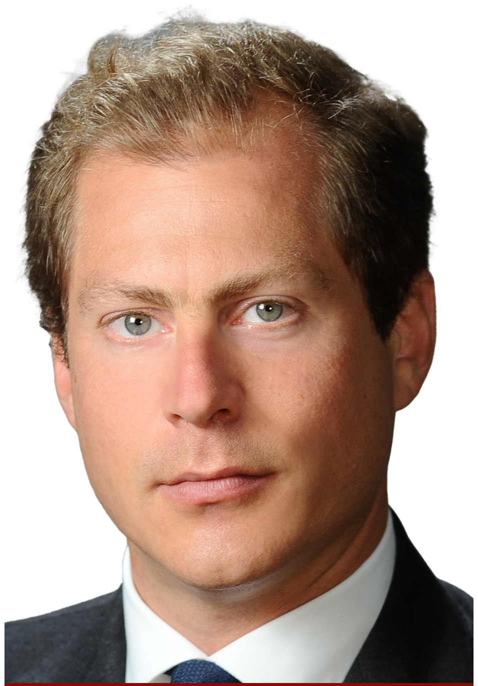
At Tikehau Capital, these trends align closely with our PE focus areas. Historically, we have focused on sectors such as decarbonisation, aerospace, and defence and cybersecurity, all of which are positioned to benefit from favourable macroeconomic and geopolitical conditions.

CONSUMER-DRIVEN SECTORS

Not all sectors are expected to thrive in 2025. Luxury and automotive companies, particularly those with significant exposure to European consumers, face headwinds. Softening consumer demand within Europe, coupled with potential disruptions in US demand, could dampen performance. Furthermore, these sectors are grappling with competitiveness challenges as products from the US and China gain market share. These dynamics underscore the importance of selective and strategic investment decisions as PE players navigate a year of contrasting fortunes across different industries.

THE YEAR AHEAD

Looking ahead, 2025 offers a landscape with significant opportunity for PE firms prepared to leverage available capital, adapt to shifting trends and invest in high-potential sectors. By aligning our investments with Europe's strategic priorities and focusing on transformative sectors, Tikehau Capital remains committed to delivering value while contributing to economic resilience and innovation. As PE continues to play a pivotal role in shaping the global economy, the year ahead promises to be both dynamic and transformative, underscoring the need for disciplined yet forward-looking investment strategies. ■



ROBERTO QUAGLIUOLO
DEPUTY HEAD OF PRIVATE EQUITY

TIKEHAU CAPITAL

ARVID TROLLE
CO-FOUNDER AND PARTNER

NJORD PARTNERS

Between 2009 and 2022, PE and the broader market enjoyed a period of prosperity driven by low interest rates, which provided cheap financing, multiple expansion, and a liquid M&A market. This environment offered a relatively high certainty of transactions, enabling PE firms to capitalise on favourable conditions for growth and profitability. However, over the last couple of years, the landscape has shifted dramatically due to a confluence of economic and geopolitical factors.

The Covid pandemic and subsequent lockdowns triggered a series of economic disruptions. Higher interest rates, inflation, and spiking energy prices in 2021 further strained balance sheets, leaving businesses with less capacity to invest in capex and growth initiatives. This has weakened positions compared to four or five years ago, making it more challenging to maintain the same level of performance and expansion.

Adding to these challenges, global conflicts and geopolitical concerns have dampened market sentiment and liquidity. Investors and businesses alike have adopted a more cautious approach, further reducing the fluidity of transactions and investments. This caution has permeated the market, affecting overall economic activity and confidence.

Despite a 9% year-on-year increase in M&A deal values in the first half of 2024, EMEA M&A volumes decreased by 26%. Activity remains significantly below the levels seen between 2020 and 2022, as well as pre-Covid benchmarks. This decline in activity has resulted in fewer exits, meaning less capital is returned to LPs. Consequently, less money is reinvested into PE funds, creating a self-fulfilling cycle of reduced liquidity and investment.

Historically, European default rates have been a reliable indicator of financial distress. While these rates remain low, there has been a notable increase in amend and extend transactions. Light covenants and a lack of lender protections have forced companies and sponsors to opt for amendments and extensions instead of traditional refinancing.

Between 2019 and 2022, the market saw an average of £3.5bn in amend and extend transactions per year, with the figure falling as low as €1.3bn in 2022. However, in 2023, this figure skyrocketed to €36bn, representing a more than tenfold increase. A similar trend has been evident in 2024, indicating ongoing financial strain.

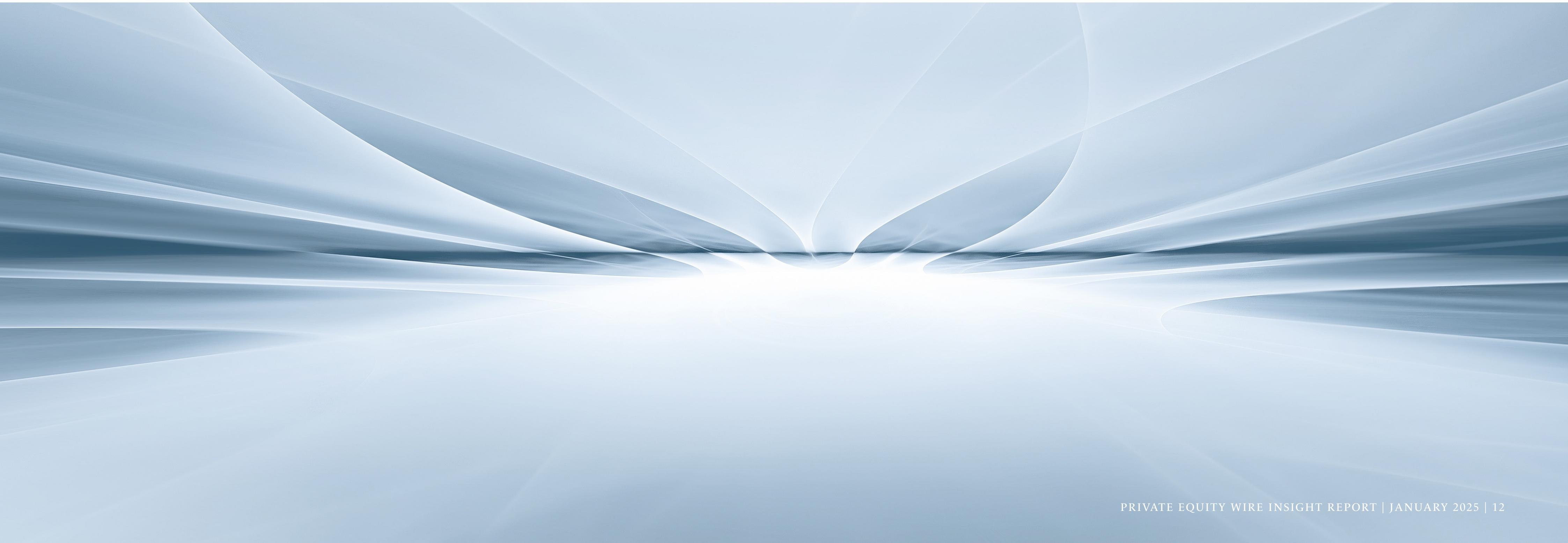
On top of this, a significant maturity wall is projected for 2025-2028. In a buoyant market, companies are able to refinance at low rates, but if current conditions persist, more amend and extends or hard restructurings may be the result as companies struggle to refinance. This increasing number of amend and extend transactions is likely to lead to more casualties, as PE firms cease to inject additional capital, and creditors become unwilling to provide further funding.

All of these factors are creating significant pressure in the system. If the economy improves and businesses perform well, those that have undergone amend and extend transactions may work themselves out of these positions. However, if economic conditions remain challenging, the lack of liquidity could lead to a higher rate of defaults and restructurings.

The interplay of economic, geopolitical, and market factors is reshaping the strategies and outcomes for PE firms. Navigating this new landscape will require agility and strategic foresight, and funds with strong experience in operational and financial restructuring will have a clear advantage if the market fails to recover in the short to medium term. ■

VALUE CREATION

Pressure on multiple arbitrage models has ushered in a new era of value creation – leading managers present their strategies



For 2025, we expect further gradual recovery in the dealmaking environment. Against the odds, central banks in the US and Europe have delivered a soft landing, and are now unwinding tight monetary policies. Despite tough fundraising conditions, unprecedented reserves of dry powder are pressuring GPs to deploy. Simultaneously, the incentive to monetise is strong: GPs are holding two-to-three times the number of portfolio companies compared to a few years ago, putting operational strain on resources.

Against this backdrop we expect 'green shoots' of dealmaking will take root, as a constructive market environment coupled with the motivation of GPs to transact will help narrow the bid-ask spread between buyers and sellers.

However, the playbook and strategy of the last cycle is not likely to drive returns going forward. Higher interest rates and lower leverage have put buy-and-build M&A strategies under scrutiny in recent years, as the opportunity for returns through multiple arbitrage is limited. In this new cycle, firms which focus on building strategic value and creating returns through EBITDA growth will truly stand out, with disciplined investment strategies and hands-on, sector-specific operational expertise really making the difference. This is something we are, and have always been, focused on, having delivered 80% of our value creation from EBITDA growth, with little reliance on multiple expansion. We have maintained clear discipline in our investment thesis, pursuing multiple value creation levers and targeting investments in sectors where our active ownership model is uniquely well-positioned to create value.

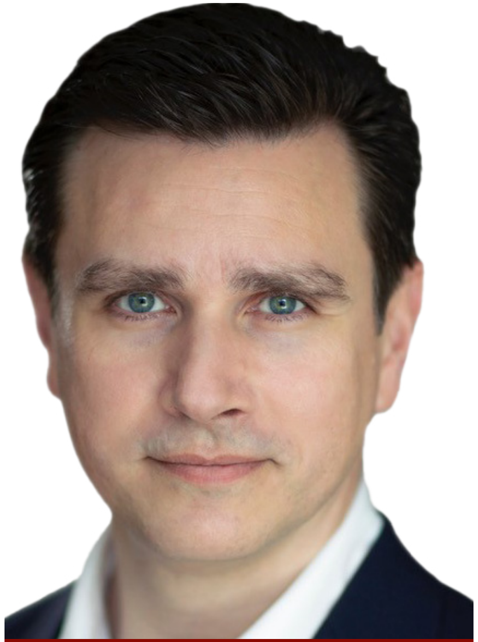
In a market that will still be in the process of re-opening, and one which will carry a degree of unpredictability, the GPs that really stand to outperform in 2025 will be those with broad exit optionality, which have demonstrated an ability to generate liquidity throughout the cycle despite market conditions. Exit optionality is inherently strongest for the GPs focused on the upper mid-market where assets are viable targets for large strategics, while record large-cap dry-powder means strong demand from sponsors and public markets can still provide an attractive path to exit for the right assets.

Over the last 18 months, BC Partners has demonstrated this, delivering significant monetisations by securing exits to a range of different buyers, delivering over €11bn to LPs. These exits include strategic buyers, large-cap GPs, family offices, and capital markets – including the successful listing of Springer Nature on the Frankfurt Exchange. This is particularly notable, given that dealmaking volumes have been down 20-30% and the IPO market remains largely closed. Driven by our strategic emphasis on exit optionality and value-add, we have secured on average a 30% uplift on valuations at exit in the last 18 months.

Value-add is equally important for LPs that have been laser focused on liquidity – especially DPI – in 2024. Firms that deliver well on metrics beyond pure IRR will validate their strategy in 2025, where sponsor-led exits look to be increasing. As many investments made in the height of the post-pandemic vintage reach maturity, LPs and peers will also be monitoring how firms have fared in a challenging environment for generating alpha.

With increasing returns to LPs, we believe the fundraising market will be incrementally better than recent years. Early successes in dealmaking, coupled with proceeds generated in 2024, will provide LPs with the confidence to back proven, cycle-tested teams to deploy in this new business cycle, without relying on an investment playbook supported by the tailwind of liquidity and multiple expansion. While PE has had several false starts on dealmaking through volatile and challenging years, the performance of 2024 positions 2025 as an opportunity for GPs to demonstrate their value-add in building better businesses.

Overall, the 2025 outlook for European PE – especially within the middle market – is optimistic. Market and macro conditions are improving, valuation expectations are being managed down, and Europe's fragmented market creates a great opportunity for those with local knowledge. Firms that navigate the evolving landscape by leveraging sector expertise, maintaining disciplined investment strategies, and capitalising on improved market conditions will achieve significant success. ■



ALEXIS MASKELL
PARTNER, GLOBAL HEAD OF INVESTOR RELATIONS

BC PARTNERS

DAN MORGAN
PARTNER

MONTAGU

Carve-out transactions, where specific business units within larger corporations are separated into stand-alone businesses, have long been a key theme of deal flow in the PE industry.

Carve-outs have become a more prominent feature of the market in recent months and we expect this trend to continue in 2025 and beyond. Macroeconomic conditions are providing significant tailwinds. With consistently higher interest rates and more liquidity constraints than we've witnessed for many years, we expect an increasing number of established companies to consider alternative sources of cash as they make capital allocation decisions, with carve-outs of non-core divisions emerging as a logical option. Supporting this trend is also a shift in corporate strategy-setting, with a focus on strengthening core competencies rather than diversification.

Carve-outs are complex transactions, which involve disentangling operations and infrastructure from a parent company, as well as understanding the dependencies with the parent business. They are far from straightforward to deliver and require skilled and trusted partners with significant operational and financial expertise and experience to execute these deals effectively. Investment professionals involved in these deals need specialist capabilities to de-risk the separation process and set the business up for standalone success.

In the last five years, carve-outs have comprised 44% of all Montagu transactions, and this share has only increased in the current higher interest rate environment. In 2024, Montagu completed three carve-out transactions, with the acquisition of Cook Medical's biotech business in January and its subsequent merger with RTI Surgical (now known as Evergen), followed by the carve-out of Medical Device Components (MDC) from Johnson Matthey. Both transactions involved Montagu's dedicated carve-out-focused operating partners.

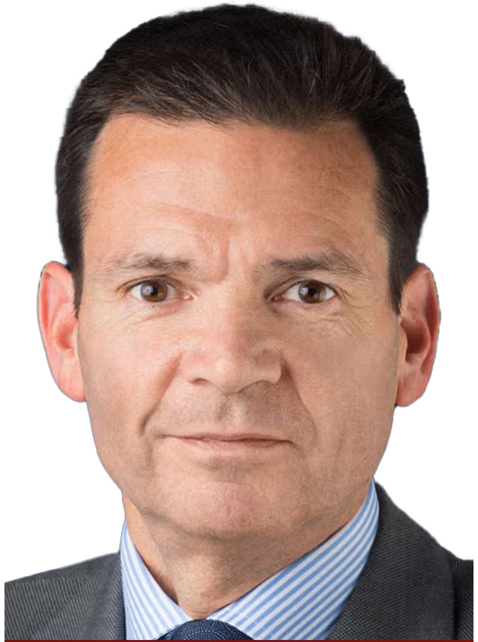
Carve-outs provide unique opportunities for the standalone company to unlock value, allowing it to concentrate on its core mission and strategic goals without competing for resources or attention with other divisions of a larger business. When executed well, it enables the company to operate with greater agility and make important investments in the business, its technology and talent, to support growth and innovation. This value creation potential continues to make carve-outs an attractive proposition for the companies as well as investors.

Looking ahead, the conditions are ripe for carve-outs to become an even larger part of the PE landscape in 2025. Corporate divestiture activity is expected to remain robust as companies grapple with capital constraints and strategic realignments. Meanwhile, the PE industry's focus on operational transformation and long-term value creation aligns perfectly with the opportunities presented by businesses that may have seen less investment and focus as a non-core part of a larger parent.

The combination of these dynamics positions carve-out transactions as a key trend to watch in the coming year. ■

RICK LAWRENCE
PARTNER

MONTAGU



GUNNAR OVERSTROM
PARTNER

CORSAIR CAPITAL

After a sustained period of prosperity, the past two years have been challenging ones for the PE industry. Higher inflation, rising capital costs, increased regulatory burdens, and a more aggressive Federal Trade Commission have collectively curtailed exit activity, constrained fundraising, and limited new deal flow. However, with improved inflation data, a dovish Federal Reserve, and a new presidential administration and congress, the outlook appears set to brighten.

With lower inflation, and a Federal Reserve that is firmly into an easing cycle, the industry's cost of capital should come down. The combination of lower inflation and President-elect Trump's stated preference for smaller government and less regulation (and a Congress that looks set to support him) should provide some scope for cost management. This same regulatory posture offers renewed hope around the industry's efforts to capture some of the $11tn sitting in defined-contribution retirement plans. Finally, a more lenient antitrust posture should ease the path to successful mergers and acquisitions of all sorts – sparking Keynes's 'animal spirits' and further bolstering the prospect for economic activity of all sorts. Together, these factors suggest a brighter future for exit activity, fundraising, and deal making.

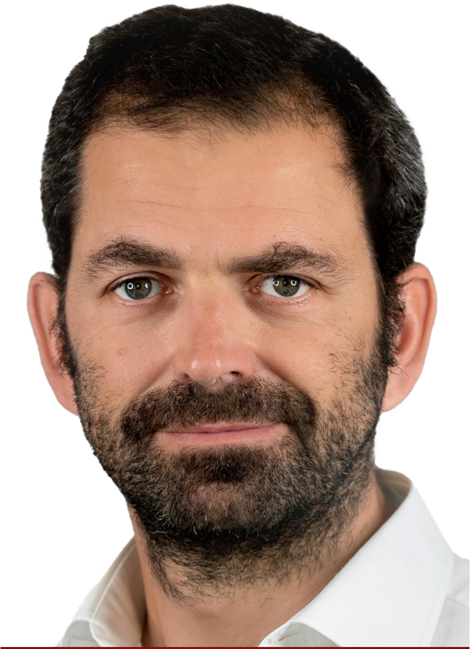
With that said, the PE industry remains intensely competitive. There are more players today than ever and the industry's 'dry powder' has reached record levels. This abundance of capital is chasing a market, in the form of mostly middle-market businesses, that has not expanded at nearly the same pace. Economic fundamentals dictate that heightened demand amid constrained supply drives up prices. This circumstance is only exacerbated by the legions of bankers and lawyers whose sole job is to ensure that every seller performs nothing less than a 'market check', if not a full-fledged auction, before transacting.

COMPETITION AND VALUE CREATION

So, in a brighter but intensely competitive market, how can a PE firm continue to generate attractive risk-adjusted returns for investors? At Corsair, we rely on well-defined and repeatable strategies for value creation across our core payments, software, and business services industry sectors. We recognise that we are going to have to pay market clearing prices to acquire well-performing businesses with talented management teams – and we know that the business-as-usual return inherent in that price will not meet our, or our limited partners', objectives. To address this reality, starting in 2012, we began assembling a team of dedicated operating partners with expertise in those functional areas where we most frequently see both opportunity and risk. These are: talent and organisational development; data and technology; and 'go-to-market'. We complement this team with industry-oriented operating partners who join us at the origination or due diligence stage of a deal and serve on our portfolio company boards until exit – aligning their economic incentive with our own. This combination of resources, working consistently together with ever-improving playbooks, gives us confidence that, even in an intensely competitive environment, we can continue to drive the operational improvements required to generate attractive risk-adjusted returns for our investors.

LOOKING AHEAD

2025 is poised to be a pivotal year for the PE industry with both higher activity in deal making and fundraising. This rising tide is likely to lift all boats and, accordingly, generate some winners that otherwise might not have fared so well. While we look forward to this period, our business is built around a sustained right-to-win and creating our own luck. We are optimistic for an eventful new year and are excited to leverage our playbook to seize new opportunities as they arise. ■



ALEXIS MEFFRE
CHIEF EXECUTIVE OFFICER

QUILVEST CAPITAL PARTNERS

In 2024, PE navigated persistent challenges across its value chain – spanning fundraising, dealmaking, and exits – amid continued economic uncertainties. Yet, the mid-market segment, particularly for firms like ours with a focus on buyouts, secondaries and private credit strategies, showed resilience.

A highlight of the year was Quilvest Capital Partners's successful exit from Metro Franchising. As one of the largest franchisees in the Dunkin' system and the largest Dunkin' franchisee in the New York City metro region, Metro significantly expanded under Quilvest Capital Partners' sponsorship. From an initial 44 units, Metro grew to 105 through seven acquisitions and 23 de novo unit openings, more than doubling its footprint across the New York City metro region and Long Island.

In the buyout space, other notable transactions included our investments in Acuiti Labs and Lunettes pour Tous (LPT). Acuiti Labs is a London-based SAP consulting firm specialising in SAP BRIM implementation for large global businesses. Founded in 2014, LPT is a French optical retailer offering affordable eyeglasses in just 10 minutes through proprietary technology. It operates 24 stores across high-traffic locations in France and Belgium.

On the primaries, secondaries and co-investments side, a standout achievement was our participation in the Summa Circular continuation vehicle as the Lead Secondary Investor for NG Group, our first Article 9 fund, which closed at the end of 2023. This innovative transaction, executed in partnership with Summa Equity, highlighted our commitment to sustainability and circular economy initiatives, providing NG with additional capital to support its ambitious growth strategy in the circular economy space.

Fundraising in the mid-market remained relatively stable, driven by strong activity in the secondaries market, where GP-led single and multi-asset transactions reached record levels and gained significant traction, despite broader market pressures.

Looking ahead to 2025, we anticipate inflation, and interest rates will continue to influence the PE landscape. In the US, we are encouraged by the prospect of further rate cuts, which could foster a more favourable investing environment, though the extent will depend on economic growth trajectories. Similarly, in the UK and Europe, rate adjustments – albeit slightly delayed – are expected to benefit consumer spending and broader economic conditions. However, geopolitical uncertainties – such as a change to the tariff landscape and conflicts in Ukraine, the Middle East, and Asia – pose potential risks, especially concerning inflation and oil prices. While these factors add unpredictability, absent any major geopolitical disruptions, we are optimistic about the PE outlook, particularly given our focus on the middle market.

In the secondaries market in 2024, we identified high-value GP-led transactions, while on the co-investment front, deal flow with attractive entry multiples remained strong. Lower middle market, sector-specialist buyout funds also presented unique embedded value opportunities on the primary side. ■

SECONDARIES

With liquidity being a top focus for LPs and GPs, learn how evolving know-how around LP-led and GP-led secondaries is fuelling deal activity

STEVEN NICHOLLS
SENIOR INVESTMENT PARTNER AND HEAD OF GP-LED SOLUTIONS

HOLLYPORT CAPITAL

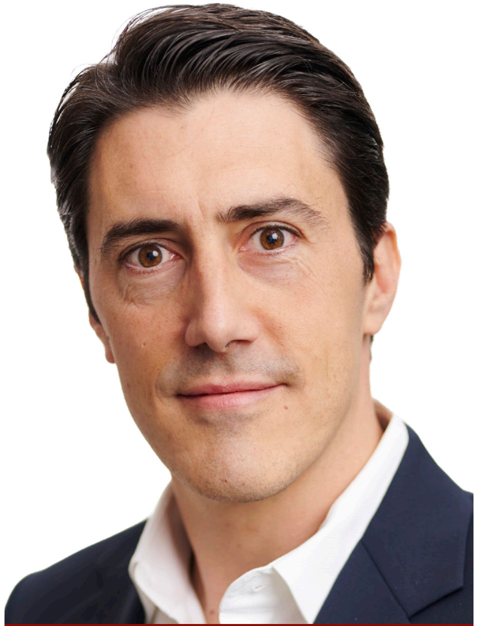
Pressure on dealmaking has been mounting as prolonged economic and geopolitical uncertainty has resulted in another year of subdued M&A activity. Yet, with the cooling of inflation and slow abatement in interest rates globally, we believe that M&A activity will bounce back and there will be greater levels of liquidity.

Secondaries are a vital source of liquidity in an inherently illiquid private equity market. Hollyport is a specialist secondary investor focused on capturing value in assets that have exceeded their initial time horizon.

The first half of 2024 saw record levels of global secondary transaction volume driven by the narrowing bid-ask spread and near-peak levels of secondaries “dry powder”. LPs continue to use the secondaries market as an active tool for portfolio management and to generate liquidity in a challenging exit environment. For the same reason, we have seen more and more GPs moving high-quality assets into continuation vehicles to allow them to capture future growth potential, while returning capital back to investors. Such transactions are now a well-accepted alternative route to exit and make up around 14% of total sponsor-backed exit volume.

When looking at GP-led transactions, Hollyport does not focus on specific sectors, but rather on the quality of a business and the capability of the management team to deliver on their strategic objectives. In 2021, we worked with Sterling Capital Partners to restructure their 2005 vintage fund which had one asset remaining. School of Rock, a franchise business operating music schools for children and teens globally, needed additional time to maximise value following slower than expected growth in the investment’s early years. The business was able to dramatically accelerate its growth plans and achieve our investment objectives within a shorter period than anticipated. We were able to exit the business in 2023 and generated a significant return for our investors, above our target for such transactions.

2024 is set to be a record year for secondary transaction volume, with advisors expecting it to exceed $140bn, up from around $115bn a year ago and from $50bn in 2014. We anticipate an acceleration of this growth in 2025, driven in no small part by the constantly evolving GP-led market. As GPs continue to seek liquidity and ways to maximise the potential of their portfolio companies, the opportunity set for investors in this part of the market is immense. What will remain key is investment selectivity and discipline. ■



INGMAR VALLANO
MANAGING PARTNER
CLIPWAY

The secondary market had a record year in 2024, with deal volume in the space estimated to total around $150bn for the 12-month period, representing a 32% increase on $114bn in 2023.

One factor behind this growth has been the lack of distributions in the primary market. Many LPs, especially pension funds, sought out the secondary market to unlock liquidity and free up investment capacity to stay active in the primary market.

As the year progressed, early signs of improvements to the macroeconomic outlook and overall market sentiment contributed to an increased alignment of buyer and seller expectations and a narrowing of secondary pricing.

A greater range and variety of new and repeat sellers came to market, looking to benefit from the improved pricing levels and secure distributions. There were also an increasing number of sophisticated sellers bringing transactions that did not involve intermediaries, which further drove deal volumes.

These tailwinds continue and we expect the ongoing narrowing of pricing to support transaction volumes in the year ahead, as well-capitalised buyers with robust appetites for LP portfolios meet sellers hungry for distributions. With greater alignment between buyers and sellers, we expect sellers to take the opportunity to exit older vintages and make up for the significant delay in DPI.

These are all good indications for the future growth of transaction volumes in the LP-led secondary market, signalling significant untapped potential for investors. It also means it is more critical than ever for LP-led secondary buyers to apply a highly selective and analytical approach to allocating capital when faced with such deep deal flow.

A DATA-LED APPROACH

As deal flow continues to increase, buyers of LP portfolios must gain a comprehensive understanding of the strategic reasons behind an LP's decision to sell and the quality of the underlying assets.

A major consideration in 2025 will be the volatility in both portfolio performance and asset valuation between different managers. To form an accurate view of the thousands of LP portfolios and hundreds of thousands of underlying assets, investors will need to be armed with extensive data analysis in order to see where the value is, and where it is not. Before assessing whether valuation multiples are reasonable, secondary buyers must underwrite portfolios and stress-test transactions at a company level. Those with a granular, bottom-up analysis of a portfolio will be better positioned to identify the underperforming assets that are sometimes overlooked as part of a 'broad stroke' approach, with a potentially significant impact on returns.

Well-integrated AI and machine learning tools will be essential for helping buyers to examine entire portfolios and understand each underlying company's growth drivers, cash flow and expected liquidity events.

The winners in 2025 will be those secondary buyers that can use advanced analytical capabilities to discriminate efficiently and effectively between data sets across LP portfolios and be truly selective when it comes to deployment. This, ultimately, will be key to achieving differentiation through performance. ■

Last year was estimated to deliver $140bn+ in global secondaries volume, the largest year on record and definitively surpassing the prior high threshold of ~$130bn in 2021, according to an early 2024 report by Evercore. The segment's growth results from a confluence of factors, including new pools of capital and entrants, proliferation of active portfolio management and a global LP base searching for liquidity. In our view, while each of these have added fuel to the fire, we believe the primary catalyst of this accelerated growth is yet another factor: the broad adoption of GP-led continuation vehicles (CVs).

The rise of GP-led transactions, which today represent nearly 50% of the market, as of early 2024 according to Evercore, is fundamentally reshaping the risk-return profile of the asset class. CVs, often centred on high-quality assets with proven performance, have the potential to deliver materially higher multiples of invested capital when compared to traditional LP-led secondaries.

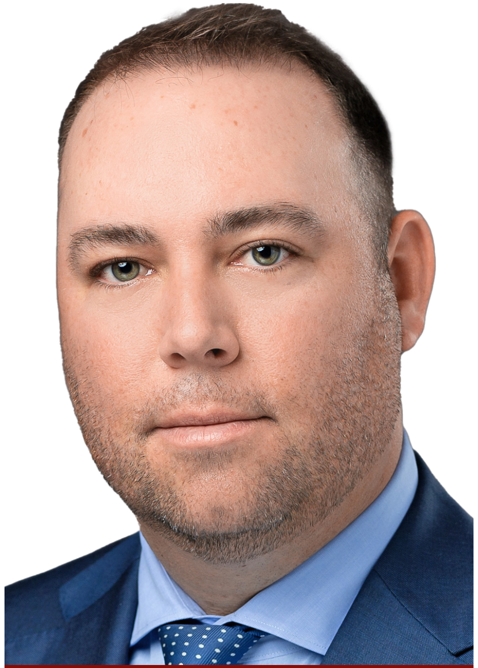
Historically, the secondary market consisted primarily of LP-led transactions, where investors benefited from j-curve mitigation, reverse vintage year exposure, portfolio diversification, and accelerating cash flows. However, Cambridge performance data for the past 20 years shows top quartile funds have taken around seven years on average to return more than one multiple on distributions to paid in capital (DPI). Additionally, average DPI in year-10 for top quartile funds was 1.4 times with an additional 40% of total gain remaining unrealised. We expect CV-focused strategies, given higher return potential and shorter hold periods, to materially outperform historical secondaries DPI benchmarks in the latter half of the fund's life.

As the embrace of GP-led continuation vehicles has broadened, we are seeing GPs utilise these structures in new and specialised ways. CV technology was originally developed on the heels of the Global Financial Crisis (GFC) to address restructuring needs. The CVs that we recognise today (associated with quality assets) took form in the 2018-2020 era as large cap sponsors leveraged them as a tool to extend the hold period of marquee assets. Since then, the market has both proliferated downstream to the middle-market and further developed into sub-categories including multi-asset transactions, end-of-fund-life cleanups, and complex mid-life situations.

Some investors have pointed to a slower exit environment and lack of distributions as a key driver of CV growth, insinuating that a material slowdown will occur when M&A returns to historical levels. However, in our view, not all CVs are created equal, and the clear benefits of the technology – allowing a GP to continue owning and compounding its best asset(s) for longer – will continue to flourish in all market environments.

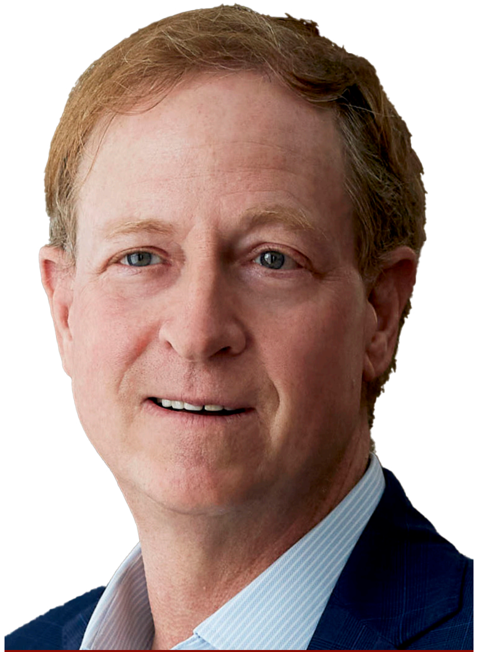
We are optimistic that the market is poised for sustained growth and innovation. Total transaction volume implies a nominal turnover rate of less than 1.5% of global private asset NAV according to the Bain & Company 2024 report, implying significant white space remains when compared to other private asset classes. Additionally, the market remains undercapitalised relative to historical dry powder-to-deal volume ratios, and we expect growing investor appetite and introduction of evergreen and semi-liquid products to fill this void over time.

Looking to 2025, we expect the market to eclipse $175bn in transaction volumes, with GP-led transactions driving a significant amount of volume, buoyed by GPs and LPs alike increasingly embracing CVs as powerful tools to generate both liquidity and attractive risk-adjusted returns. ■



NICK LAWLER
MANAGING DIRECTOR,
HEAD OF SECONDARIES

CHURCHILL ASSET MANAGEMENT



JOSEPH MARKS
SENIOR MANAGING DIRECTOR
HEAD OF SECONDARIES

CAPITAL DYNAMICS

Secondaries have always been about trying to provide liquidity, but this is the first time that an acute logjam is forming in the pipeline, taking the shape of nearly 30,000 private portfolio companies with over $3tn of net asset value that need to, or should, be sold.

LPs are having the worst several years of distribution since the Global Financial Crisis (GFC). And managers are all-hands-on-deck to provide their investors with more liquidity.

SECONDARY MARKET DRIVERS

The big change for secondaries is around the innovation and explosion of the GP-led market.

Secondaries were historically considered the problem children – the remaining assets that could not be sold back in the GFC, which is how the term zombie funds came about.

Covid transformed the landscape – it was a period of high uncertainty in which liquidity dried up. With buyers having to change their approach, we saw the GP-led segment go from a small fraction to almost comprising half the market.

The real shift, in terms of liquidity as a tool for managers, is the rise of continuation vehicles, which are growing in profile – making up 40-50% of the secondary market since the pandemic, half of which is accounted for by individual assets.

Now, managers can take assets and hold them for longer while providing liquidity for investors, increasing DPI and taking control of their liquidity profile. That represents a win-win-win for financial innovation and will likely become a permanent part of the liquidity triad – with IPO and M&A being the other two. Sponsor-to-sponsor transactions used to be the third.

EXPECT GROWTH

Metrically speaking, the embedded value on the ground between NAV and open commitments is approximately $20tn. When considering this market opportunity, the secondary market – expected to surpass around $150bn in assets this year – continues to occupy a small fraction. Accounting for the continuation vehicle space, which is outpacing the overall landscape, we are poised for a period of non-linear growth.

MAKING THE MOST OF THE MARKET

In a maturing market, even if it is still embryonic, there are a lot of players, but there is also plenty of opportunity for differentiation – transaction sizes, diversified exposure vs GP-led deals, geographical diversification, and so on.

What works well for us is having a primary platform and investment insights available. Secondaries are an information business, which requires sourcing opportunities outside the auction market where you can.

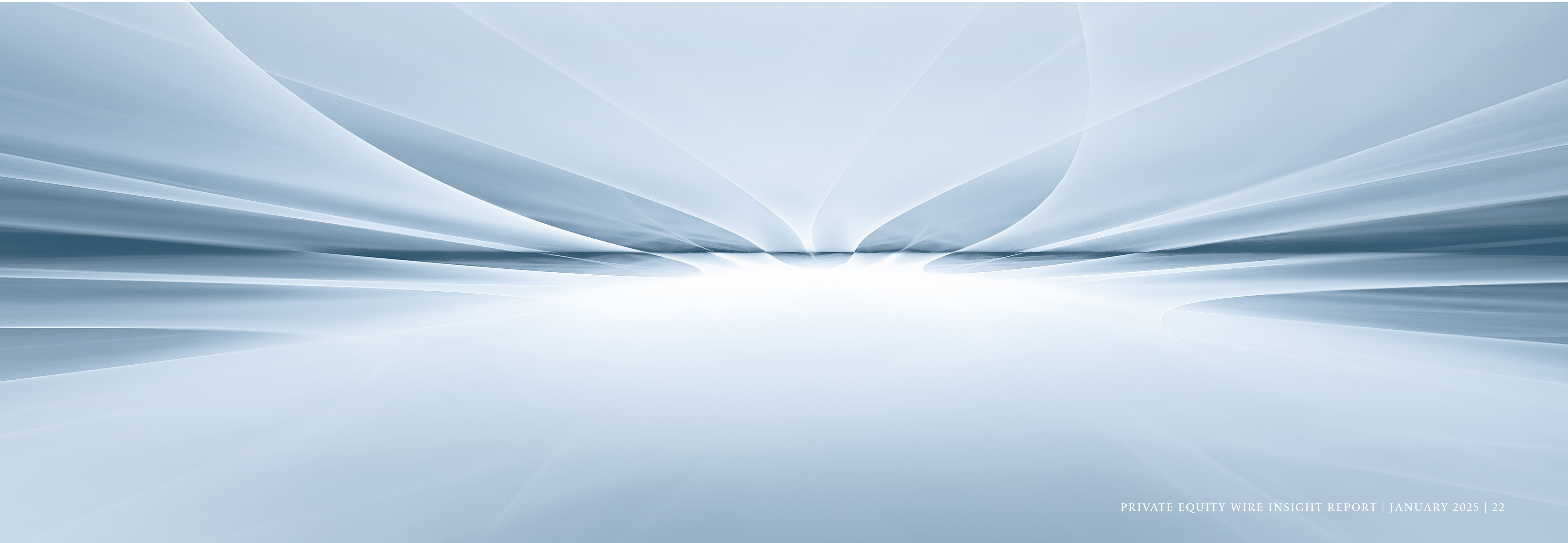
Another differentiator is relationships – something we prioritise at Capital Dynamics. With secondaries, you may have a source on a deal or good information, but you need GP access to purchase those interests or make room in an oversubscribed continuation vehicle. With good relationships, firms can stand out amongst competitors when it comes to information, underwriting, business insights, and value creation models. These are key critical factors when underwriting secondary transactions.

Finally, at Capital Dynamics, we also focus on smaller transactions. As funds get larger, it creates room for more players focusing on the smaller, more fragmented end of the market. Many transactions are not coming through the auction channel, which is very favourable – growing markets make opportunities for new entrants that tend to be smaller and often lack decades of primary investment relationships with managers.

That's the sweet spot. That's where funds with established relationships that focus on the small, fragmented transaction space – where deals can be sourced outside of the auction market, or bilateral transactions can be negotiated – will see opportunities. ■

CREDIT

Much has been made of the astronomical boom in credit, but where will the opportunities lie as the market saturates? Hear from leading lenders



With spreads in both public and private credit markets close to all-time high levels of tightness, allocators will have to be discriminating to ensure that they are being adequately compensated for the credit risk they are taking on. Recent fundraising in private credit has been disproportionately skewed towards direct lending strategies, where we believe the conditions for a period of higher dispersion in both asset- and fund-level outcomes are now in place. Higher-for-longer interest rates, muted deal volumes and excess capital in more commoditised strategies may result in adverse selection, particularly where new entrants with less well-developed sourcing capabilities have raised significant capital and are now compelled to deploy. Competition in larger deals is driving spread compression and concessions on covenants and documentation, which limits the downside protection and has been an important characteristic of the asset class for allocators.

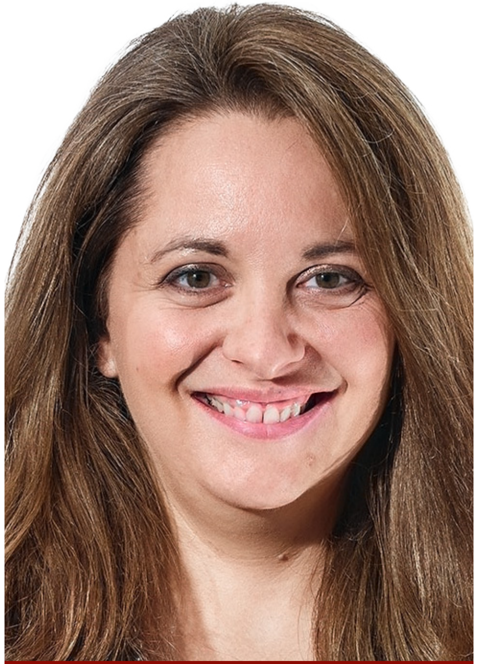
While reported default rates in private credit strategies remain low, the incidence of extensions, amendments, and capital injections from sponsors is rising as more marginal borrowers manage the effects of a persistently higher cost of capital. With interest rates now expected to remain higher for an extended period, it is likely the number of credit issues will begin to increase, leading to more amendments and restructurings, if not outright defaults.

While direct lending should remain a core component of a private debt allocation, we believe these factors are likely to lead to higher dispersion in outcomes at both the asset and fund level over the next three-to-five years. Manager selection will therefore be critical to maintaining high quality, risk-adjusted returns.

Despite significant inflows into corporate lending strategies, specialist strategies and newer managers remain capital constrained, creating an opportunity to generate higher returns by acting as a provider of liquidity. We see a secular opportunity developing in asset-backed credit as banks reshape their balance sheets in response to both regulatory and commercial pressures. Given the breadth and range of assets affected by this trend, the scale of the potential asset transfer from banks to the private markets over the next 10 years could mirror that of direct lending post the Global Financial Crisis. This not only creates a long-term opportunity for scale players in asset-backed financing, but also for smaller managers able to underwrite more esoteric assets. Similarly, the opportunity in real estate debt is likely to be persistent, particularly in a higher-for-longer environment and one in which the banks' reduction in their exposure to riskier real estate lending is likely to be permanent. Managers that can be opportunistic are best placed to benefit from this dynamic.

Given these dynamics, we believe investors with the capacity to allocate to single-sector funds, to more complex strategies, and to emerging managers may be able to achieve a better risk-return profile for their portfolios by taking a multi-strategy approach and leaning into compelling opportunities in specialist lending, asset-backed lending, and real estate as a complement to their traditional corporate lending exposures. ■

Please note: The information provided herein is for informational purposes only and does not constitute investment advice. Investors should seek independent financial advice before making investment decisions.



EMMA BEWLEY
PARTNER & HEAD OF CREDIT

PARTNERS CAPITAL

STUART MATHIESON
HEAD OF EUROPE & APAC PRIVATE CREDIT & CAPITAL SOLUTIONS

BARINGS PRIVATE CREDIT

M&A will remain a key factor to watch in 2025, and there are reasons to believe it may be poised to pick up after a slow 18-24 months. Particularly in Europe and North America, clarity is improving, and we are beginning to see positive trends around deal volume.

Looking at our global portfolio of 350+ companies over the last year, there is a notable mix of new platform deals and 'off-market origination', or add-on transactions in which we have provided additional financing to sponsors or companies we've lent to previously. While a stronger M&A environment would certainly be positive, incumbency matters and will continue to drive significant origination and opportunity as sponsors grow their investments.

THE MIDDLE MARKET

Middle market companies have held up well in the face of challenges – not only from higher interest rates, but also from higher inflation, labour shortages, and supply-side shortages. The combination of high prices and elevated interest rates will continue to put pressure on cash flows, perhaps to a greater extent in the UK than in Europe, as UK rates are expected to be higher for longer. But companies that have been able to adjust and adapt so far should continue to fare well.

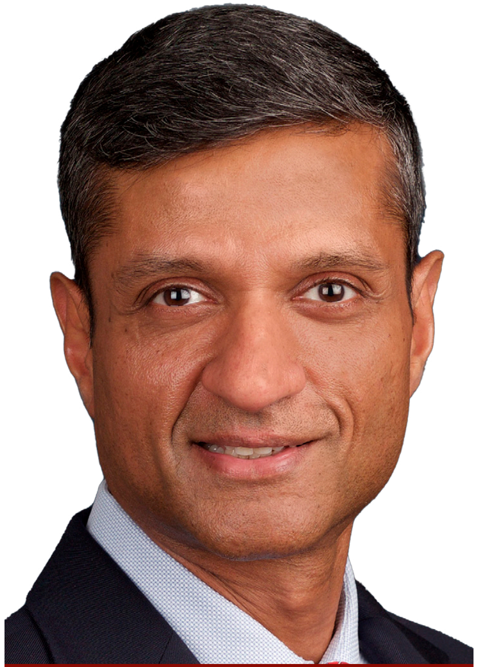
Regarding capital structure resilience, the vast majority of our lending is around a sponsor-led buy-and-build strategy, where capital structures are positioned for flexibility rather than simply to maximise leverage. To execute that strategy, you have to be in a position where you can draw down a facility at a point in time when a company or sponsor wants to buy an asset, and that can be more challenging with a stretched balance sheet. That's a key benefit of the core middle market generally – capital structures tend to be more conservative, with value drivers coming from operational improvements and buy-and-builds, rather than leverage.

DEAL TERMS

In Europe and North America, there has been an influx of new managers in recent years, many of which are what we refer to as 'asset collectors'. These are typically either new entrants that lack the ability to scale or lead deals, or lenders that have continued to raise larger funds and target bigger transactions. In a competitive environment, asset collection can lead to challenges when it comes to deploying capital, and lenders in some cases have consented to less favourable deal terms as a result. Specifically, for some larger private transactions that could be financed in the public markets, margins have compressed with structures and documentation weakening as well.

In the core or traditional middle market, terms have remained quite favourable. Traditional, first-lien senior debt tends to be more insulated from the risks associated with the growth of large private market deals. Documentation and covenant protections in this part of the market also tend to be more robust. The spread premium that the middle market has historically offered over broadly syndicated loans has remained compelling as well, despite spread compression. The premium in Europe is up from last year and still attractive, in our view, considering where rates are today.

Long-term financing needs can extend beyond senior direct leveraged buyout lending to areas like capital solutions, portfolio financing, asset-backed finance, and equity co-investments – all the way to public credit market financing support. Ultimately, lenders with the capabilities and breadth to support these requirements are in a good position to serve as strategic partners to sponsors and source differentiated opportunities for investors. ■



NIK SINGHAL
GROUP HEAD OF DIRECT LENDING

ORIX CORPORATION USA

We view middle-market direct lending as a long term multi-trillion-dollar durable asset class. We do not view it as a point in time trade, or a flavour of the year strategy, and neither should investors.

However, looking more narrowly at current market conditions, we believe the anticipated rate cut cycle will be a huge positive for the middle market. Over the last two-to-three years, the trifecta of high inflation, high interest rates and low revenue growth has hampered businesses. Today, inflation is almost back to normalised levels, and interest rates have started to come down. With these two headwinds gone, I see two major positives:

The first is profit margin expansion for businesses, helping free cash flow generation. The second: lower cost of capital driving dealmaking and M&A activity, fixing the temporary imbalance between availability of capital and avenues for deployment.

We expect 2025 will present the right conditions for this, driven by further rate cuts and the enactment of business-friendly policies and decreased regulation by the new administration

Cuts amounting to 75 basis points since September are not one-off, but the beginning of a rate cut cycle. With inflation now under control, further rate cuts are not only justified but also necessary to promote economic growth. As of right now, markets are pricing in another 70 basis points of rate cuts through the end of 2025. My view is that despite some initial tough tariff talk by the incoming administration, their policies will largely be supportive of keeping inflation in check, and likely bring it down even further. In other words, the market is likely underestimating the extent of fed cuts next year. A reduction in cost of capital is and will continue to be a positive development for middle-market businesses.

A large amount of PE dry powder has been waiting on the sidelines. As this capital gets put to work, sponsors will need flexible financing solutions from their lenders, coupled with speed and certainty of execution. This anticipated demand will fix the current temporary supply/demand imbalance in direct lending – that is, the perception of too much capital chasing a few deals.

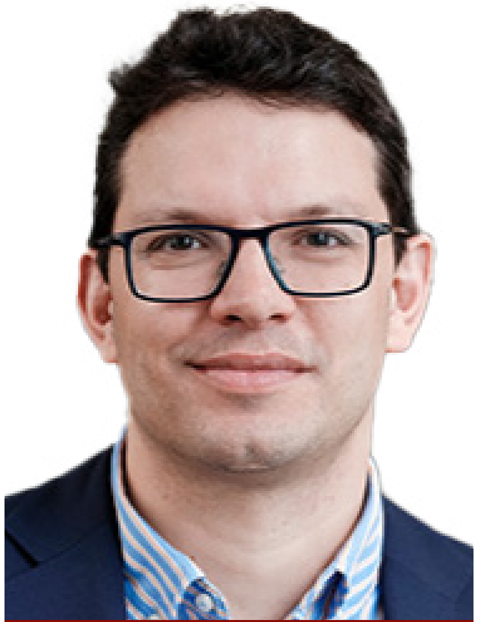
Direct lending, and even middle-market lending, are now very broad asset classes. So, investors looking for opportunities will be well served by having a narrower focus. Our focus is on sponsor-backed, first-lien only, lower middle-market lending. This market is relatively uncrowded compared to upper and core middle market and has continued to maintain its investment discipline and structural protections.

In terms of a longer-term outlook, market conditions will naturally fluctuate over time. Rather than try to time the market, investors should focus on selecting high-quality managers where scale is important, but skill is even more critical. And skill is three core things: deep industry and sponsor relationships; workout expertise; and quality of documentation

Finally, direct lending investors will be well served to select managers that not only possess these skills but also have a lot of skin in the game themselves. ■

MEGA TRENDS

Future investments align with global mega trends – digitalisation, the energy transition and supply chain reorganisation. Hear from Impact and infrastructure investors



NICOLAS MULLER
MANAGING DIRECTOR,
HEAD OF PRIVATE EQUITY
PARTNERSHIPS

BLUE EARTH CAPITAL

Looking towards 2025, we believe that the landscape of impact investing is poised for significant evolution, even against the backdrop of ongoing macroeconomic uncertainties. More than ever, a long-term investment horizon is crucial for intentional impact allocations. Impact managers will need to offer innovative strategies that are resilient to short-term volatility and address long-term structural environmental and social challenges.

As the market matures, impact investors will begin to encounter similar challenges as other private capital investors, and we must adapt our strategies accordingly. In a generally slow exit environment for private market assets, LPs are increasingly focusing on DPI – and impact investors must demonstrate their ability to deliver realised returns if they wish to raise new and larger funds in 2025. In this context, impact secondary transactions have begun to emerge as a vital tool for creating liquidity for investors, ensuring capital continues to flow to impactful ventures.

As a dedicated global impact investor, Blue Earth Capital operates at the forefront of the impact movement. We are committed to leading the development of an efficient secondary market for impact investments, as we consider secondaries to be a key driver of the continued growth of impact investing which can allow investors to deliver meaningful impact alongside realised returns.
As an example, in January 2024, we completed a landmark transaction in partnership with British International Investment (BII), acquiring a partial interest in three of BII's existing funds. This strategy, the first of its kind in the sector and the first involving a Development Finance Institution (DFI), serves as a real-life example of how secondaries can be used to catalyse new investments in emerging markets.

Despite a volatile political landscape and economic pressures, climate investing will remain a core focus of impact investors, including Blue Earth Capital, in 2025. The urgency of addressing climate change continues to galvanise private capital towards sustainable solutions, and we are committed to supporting companies that accelerate the energy transition and address broader environmental challenges. This commitment extends beyond tackling greenhouse gas emissions and achieving net-zero goals. A pressing example is the worsening global water crisis. Freshwater use has grown by 130% since the 1960s, according to a World Resources Institute report from 2020, while supply has declined by 602% – according to BNP Paribas. In the face of this urgent challenge, water will be a key investment theme for Blue Earth Capital in 2025.

Blue Earth Capital will also continue to focus on social impact investments, particularly inclusive growth and access to essential services. Almost 700 million people still live in extreme poverty, the World Bank reported in 2024, mostly in developing countries. Investments in financial inclusion, healthcare, education, and job creation remain critical to ensure prosperity and sustainable growth, especially across emerging markets. Our investment in Tyme Group exemplifies this commitment, expanding access to affordable financial services in Africa and Asia.

While 2024 has been a breakout year for impact investments, we believe 2025 will reward managers that remain at the forefront of this growth. It will be increasingly important for managers to develop and scale strategies that not only meet demand but also anticipate it. By developing and deploying innovative structures, they can unlock capital inflows and deliver tangible impact. At Blue Earth Capital, we will remain steadfast in our commitment to our 'total impact' approach, tackling some of the world's most pressing social and environmental challenges while aiming for measurable, real-world impact alongside market-rate returns. ■

At the time of writing, 2024 is on track to be the warmest year on record. The World Meteorological Organization's 'State of the Climate 2024 Update' was released on the opening day of COP29 in Baku and sounded a stark warning about the alarming acceleration of climate change. The report underscores the grave threat to the ambitions of the Paris Agreement, which are increasingly at risk.

That said, it is encouraging that climate action is becoming increasingly considered within PE, and private markets more broadly. Firstly, to transition to a low-carbon economy there is a need for climate solutions, and PE is well positioned to support the development and scale-up of these solutions. We are noticing an increasing number of firms incorporating decarbonisation into investment management decisions and expect this trend to continue in the years to come. In addition, we also expect that transition finance will open real value creation opportunities for companies adopting a more proactive approach. In a recent study, McKinsey identified 11 pools of potential value that could be worth between $9tn and $12tn of annual revenues by 2030. These pools include the likes of transportation, buildings and power.

Integrating climate considerations into portfolios, however, is not always straightforward, and private markets have been facing similar challenges to the wider investment community. Coupled with the rise of tighter regulation such as the European SFDR, or to the ESG backlash in the US, we are witnessing investment firms become increasingly cautious about publicising details of their climate targets or disclosing their investment approaches. However, we believe that to advance the adoption of climate-solution investments, this transparency is critical. With private markets representing a sizeable part of economies, and as such being integral to advancing towards net zero, it is important for PE investors to ensure that GPs measure and report GHG emissions data for their portfolio companies. This enhances transparency to investors, helps to assess climate risk and can pivot engagement to the areas where most impact can be made.

To evolve our understanding of the carbon emissions data in our PE portfolios, Stafford began an 18-month project in early 2023. This project covered more than 80 managers and 500 portfolio companies. We collected data on Scope 1, 2, and 3 emissions, company emission targets, emission estimate inputs, net-zero alignment, and decarbonisation pathways. The assessment was aimed at enhancing our understanding of each portfolio company's role, intentions, and progress towards net-zero commitments and targets, as well as to improve the quality of carbon emissions data for our portfolios. As anticipated, we observed significant discrepancies between the estimated emissions data provided by third-party sources and the data obtained directly from managers. Accurate and comprehensive data is particularly critical for investors tracking financed emissions against interim targets or looking to implement new climate-focused investment strategies.

While there are clear differences across regions and segments of the PE market when it comes to capturing emissions data, the industry is making progress through the implementation of standardised reporting frameworks and alignment scales (such as the ESG Data Convergence Initiative (EDCI) and the Private Markets Decarbonization Roadmap (PMDR)).

There is still a gap to close. Recent data from BCG showed that only 22% of PE-owned companies have a decarbonisation strategy in place versus 29% of public companies. However, when these companies do have a plan in place, action can advance faster than within public companies, demonstrating the crucial role that PE is set to play in the years ahead.

NIELS BARDELMEIJER
PARTNER, PRIVATE EQUITY

STAFFORD CAPITAL PARTNERS

CYRUS GENTRY
MANAGING DIRECTOR

STONEPEAK

In 2024, more than 70 countries around the world held national elections – including the US – and those elections in turn brought many questions about what 2025 will hold, not least of which is how the US will tackle its infrastructure needs over the coming years. However, putting policy to one side, there is one thing we can say with more confidence: it is estimated that nearly $100tn of investment will be needed by 2040 to modernise or replace the world's infrastructure, including in the digital, transport, and energy sectors. This represents a golden era of opportunity for infrastructure investors such as Stonepeak, the largest independent infrastructure specialist in the world, with around $70bn of AUM.

Long gone are the days when infrastructure investing was limited to airports and toll roads. Today, the market has evolved into something far more sophisticated. At Stonepeak, we divide the asset class into three key sectors: digital infrastructure – the hard assets such as data centres, cell towers and fibre networks that form the backbone of the internet; transport and logistics – the critical services such as ports, aviation and cold storage that move goods and people around the globe; and energy – the evolving sources of power such as natural gas, wind and solar energy and battery storage that support our daily lives.

We anticipate that each of these sectors and associated investment activity will grow rapidly over the coming years, driven by global megatrends that are creating significant tailwinds within each of them, namely digitalisation, supply chain revitalisation, and energy transformation. These megatrends will continue shaping the world and the economy not just next year, but for many years to come. It has already been a very robust deal-making environment within infrastructure over the past twelve months, and we only expect that to continue into 2025, particularly once asset owners and the capital markets have had time to process the outcome of the 2024 US election.

At the same time, we are seeing greater interest in infrastructure from both institutional and individual investors alike. With lingering uncertainty over interest rates and inflation, infrastructure has continued to represent a compelling place to put capital to work. In addition to performing essential services, infrastructure assets typically feature high barriers to entry and few substitutes, predictable cash flows underpinned by long-term contracts, and strong pricing power. It's these characteristics that often enable infrastructure as an asset class to offer attractive risk-adjusted returns in a range of macroeconomic and inflationary environments. Infrastructure can fill a differentiated niche in investors' portfolios due to this relative stability and predictability, ultimately offering the prospect of equity-like returns for fixed income-like risk.

As a result, institutional allocations to infrastructure have been steadily increasing since the early 2000s, with global institutions dedicating around 3% of their overall portfolios to the space – a level which we only expect to rise in the coming years. Meanwhile, private infrastructure is also becoming increasingly accessible to the wealth market, including family offices and high net worth individuals around the world, through products specifically designed with their needs in mind.

It's not surprising that more investors are getting involved in infrastructure, given the way the asset class has performed. Over the last couple of decades, for example, infrastructure assets have proved to fare relatively well in inflationary, high interest rate environments. No matter the political or economic landscape of 2025, we expect another year of significant investment activity and growth in infrastructure – a challenge and opportunity which we are excited to continue to pioneer. ■

CONTRIBUTORS:

Aftab Bose
Head of Private Markets Content
aftab.bose@globalfundmedia.com

Mary Hurley
Junior Content Editor
mary.hurley@globalfundmedia.com

Johnathan Glenn
Head of Design
johnathan.glenn@globalfundmedia.com

FOR SPONSORSHIP & COMMERCIAL ENQUIRIES:

sales@globalfundmedia.com

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