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PANTHEON **PERSPECTIVES**

THREE KEY THEMES **FOR PRIVATE MARKETS IN 2024**

Contents

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Pantheon Perspectives:
Three key themes for private markets in 2024

In the ever-evolving realm of private markets, 2024 presents opportunities and challenges. In this edition of Pantheon Perspectives, we provide an overview of the macroeconomic backdrop, before delving into three pivotal themes we believe will be prevalent in 2024:

1. **Intensified focus on manager and thematic asset selection against a backdrop of continued financing pressures and expected dispersion of returns**
2. **Potential for dealmaking to be unlocked across private market asset classes**
3. **Compelling secondary opportunities amid sustained liquidity demand present strategic imperative**

Macroeconomic Picture: Balancing Act in a Shifting Landscape

Growth

Reflecting on growth forecasts from the beginning of 2023, the economic landscape has proven more robust than anticipated. The US and Eurozone both outperformed initial predictions, with the US reaching 2.5% growth year-on-year as of December 31, 2023[1]. However, 2024 forecasts hint at a dip in growth, setting the stage for more moderate economic expansion.

Central banks now face the delicate balance of managing adjusting rates and taming inflation to prevent a potential recession, which is not yet off the table in key developed economies.

Figure 1:
2023: January forecasts vs. actual growth rates[1]

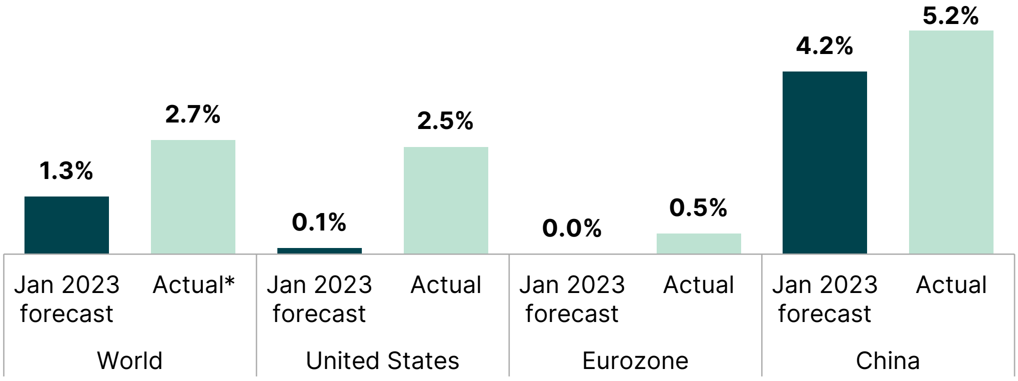
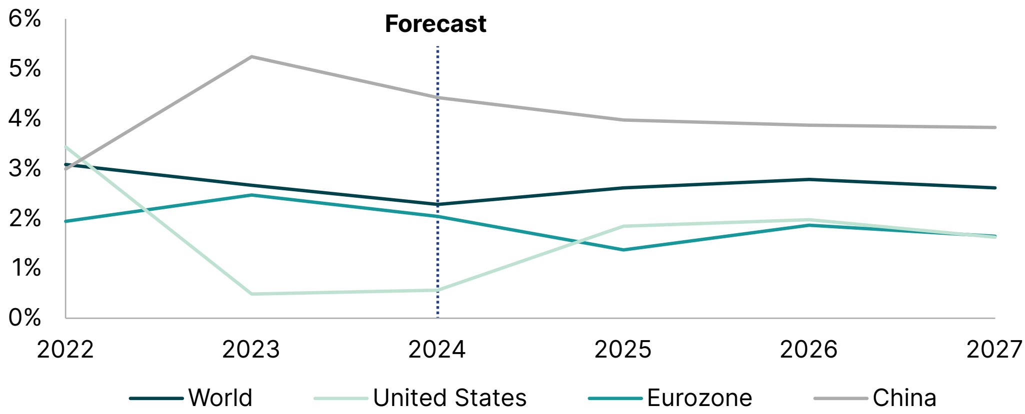


Figure 2:
Current forecasts for 2024 to 2027[1]



[1] Oxford Economics, current forecasts as of January 2024. Actual, achieved figures are advance estimates and are subject to change. * Figure is comprised of a combination of published hard data and forecasts for Q4, with some underlying countries' Q4 figures still outstanding. The forecasts highlighted are for information purposes only. There is no guarantee these forecasts will materialize.

Inflation and rates

Inflationary pressures, which gripped the US and Europe throughout 2023, have receded and are expected to moderate further in 2024. However, central banks, cautious of the pitfalls of a hasty rate cut, may take their time in bringing rates down from their 20-year highs. The Federal Reserve's projection of a 75 basis points cut in 2024[2] underscores the cautious approach to monetary policy – and "higher for longer" has become a consensus forecast.

Figure 3:
Inflation[3]

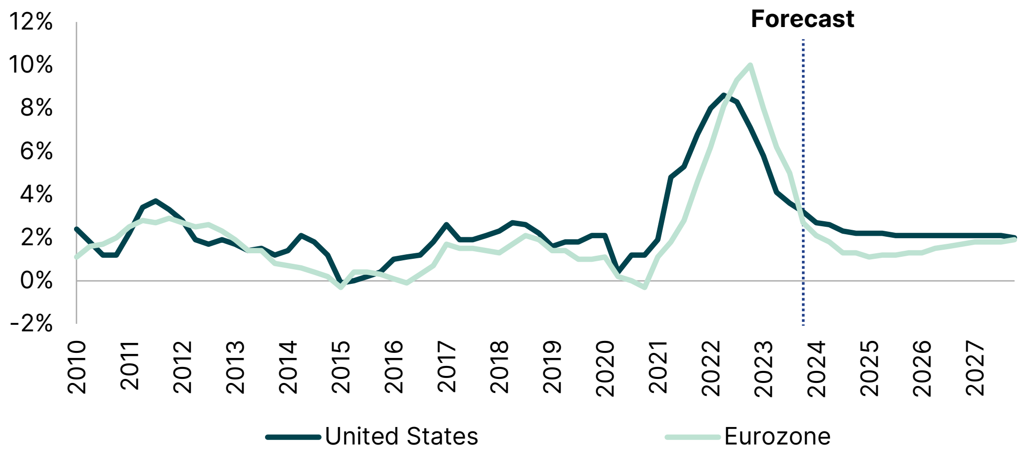
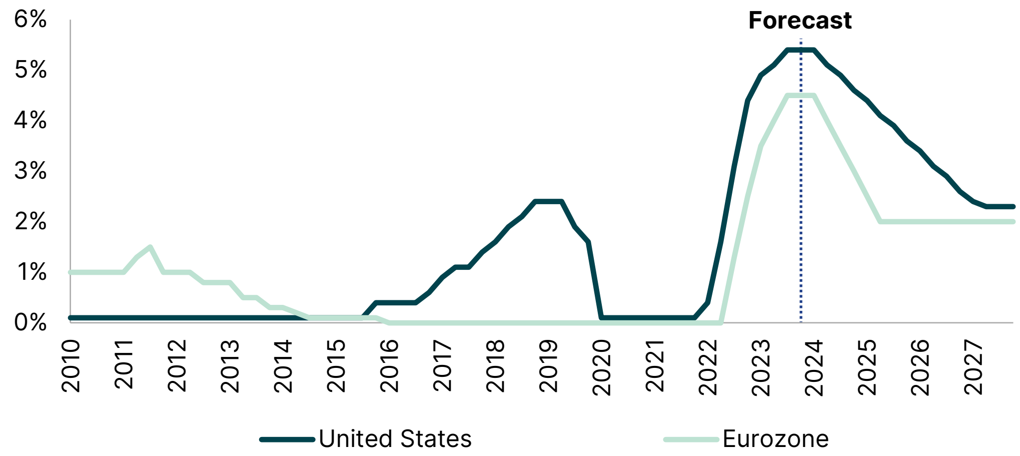


Figure 4:
Rates[3]



[2] Federal Reserve Board's Summary of Economic Projections, December 2023. 'Dot plot' charting Federal Open Market Committee (FOMC) members' assessments of appropriate monetary policy implies rates will fall 75bps by the end of 2024. The forecasts highlighted are for information purposes only. There is no guarantee these forecasts will materialize.

[3] Source: Oxford Economics, January 2024. There is no guarantee forecasts will be realized. The forecasts highlighted are for information purposes only. There is no guarantee these forecasts will materialize.

Public markets

Public markets, having weathered the storms of 2022, are cautiously optimistic as they factor in potential rate cuts. Equity markets have stabilized after a rocky period post-pandemic and showed significant gains in 2023, especially as sectors such as technology recovered following sharp declines in the previous year, while fixed income markets showed improvements in 2023 after years of muted performance. However, the threat of increased volatility looms if market expectations are not met.

Figure 5:
Public Equity Markets[4]

Listed equity markets have stabilized over 2023 after a rocky post-pandemic recovery...

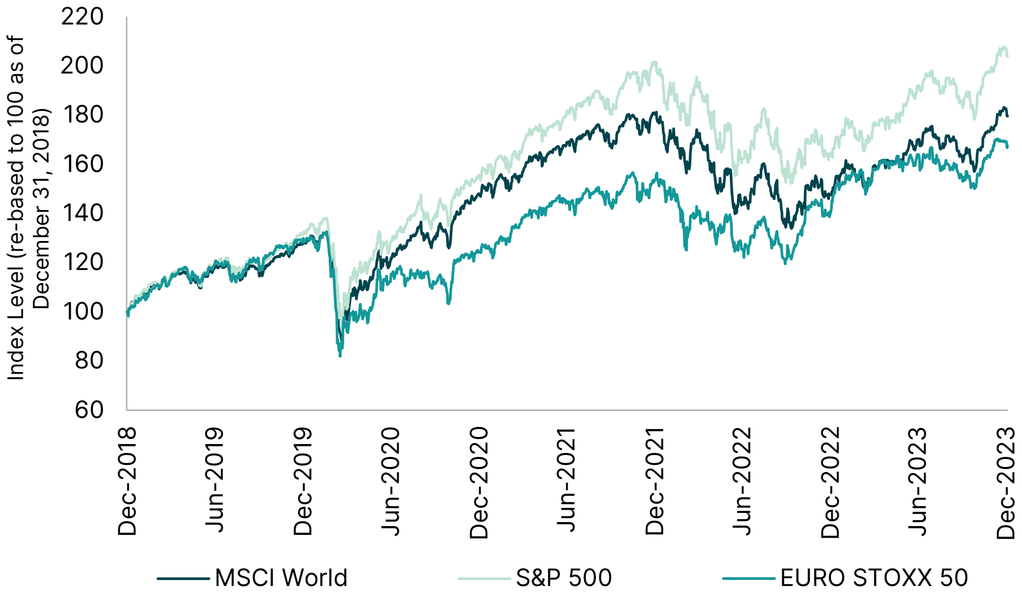
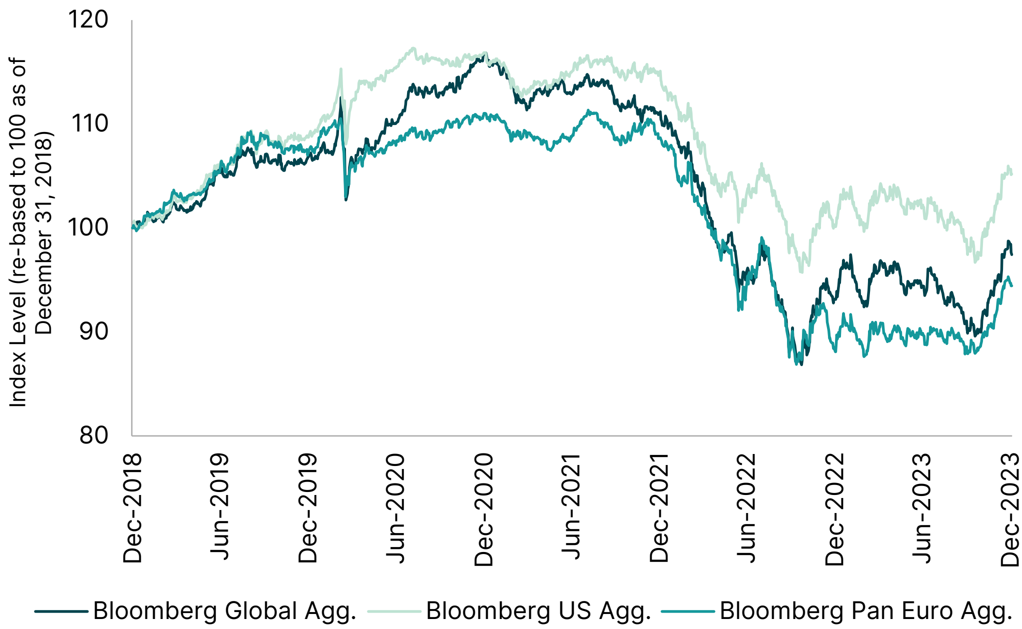


Figure 6:
Public Fixed Income Markets[4]

...while fixed income has shown recent improvements after years of muted performance



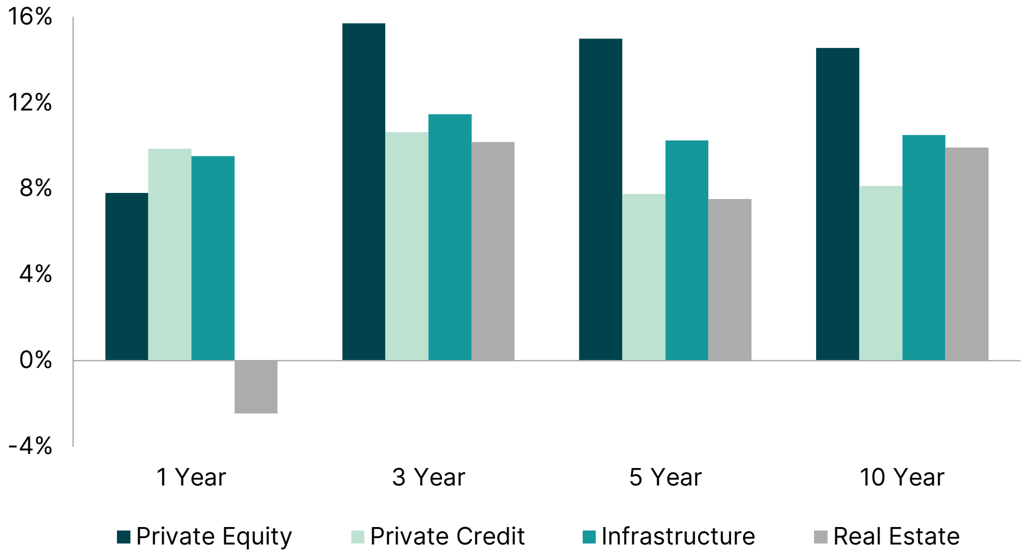
[4] Source: Refinitiv and Bloomberg as of December 31, 2023. Past performance is not a guide to future results. Future results are not guaranteed and loss of principal can occur.

Three Key Themes for Private Markets in 2024

Theme 1: Intensified focus on manager and thematic asset selection

Amid interest rate hikes, private markets face a nuanced environment shaped by the residual impact of elevated financing costs. This has resulted in a more mixed picture for returns. Taking in the bigger picture, 1-year horizon returns reflect the choppier environment that we have seen over the past 12 months. However, long-term performance continues to be strong, as shown in the 3, 5, and 10-year returns (annualized). Ultimately, this is not too surprising as we have witnessed markets adjusting to the new rates regime, but we believe that 2024 may bring tailwinds for private market performance as rates recede.

Figure 7:
Horizon Returns by Asset Class[5]



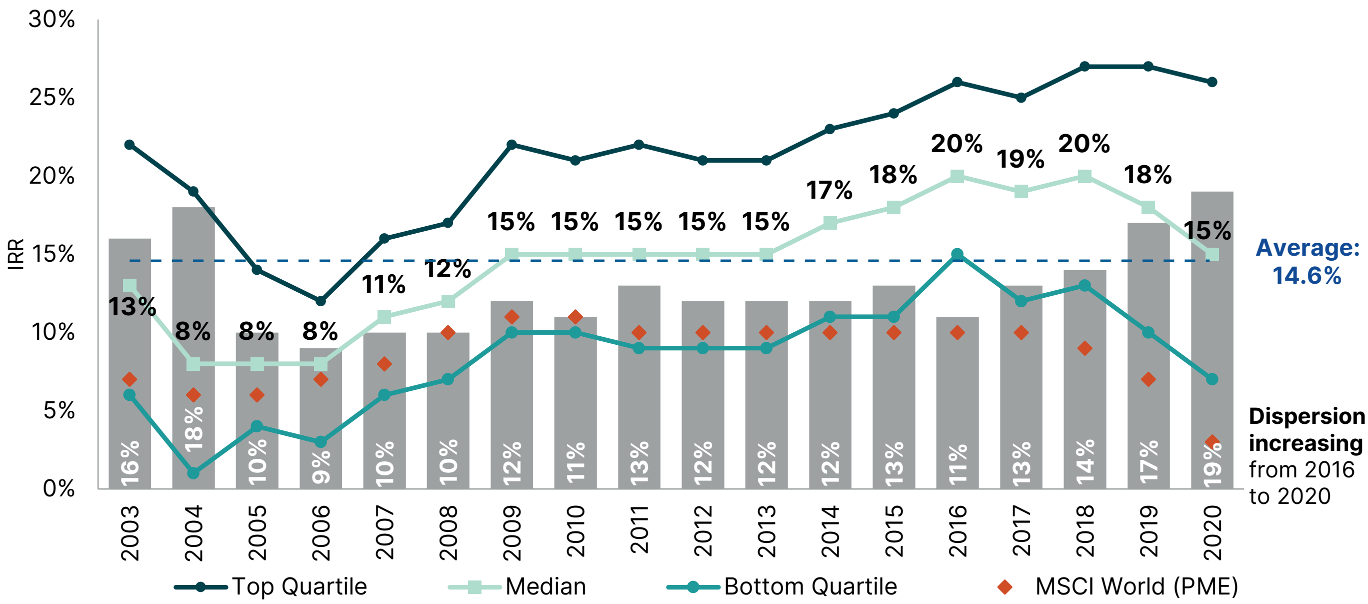
[5] Source: Cambridge Associates as of September 30, 2023. Horizon returns are pooled IRRs as of Q3 2023; Periods over 1 year have been annualized. Past performance is not a guide to future results. Future results are not guaranteed and loss of principal can occur.

Private equity

In the chart below, we can see that the performance of recent private equity fund vintages has been impacted by financing costs. That being said, median returns in private equity have remained above long-term averages – and well above the returns of the MSCI World benchmark on a PME basis – while top-quartile returns have remained resilient in the mid-20% range.[6]

As a consequence, in the most recent vintages, return dispersion has risen. With higher financing costs putting downward pressure on the levels of leverage that can be used in deals, more onus now falls on GPs to generate greater value using alternative levers. This, in turn, places heightened emphasis on manager selection; being invested with the highest quality GPs and benefiting from their ability to drive operational value becomes increasingly important.

Figure 8:
Private Equity Fund IRRs by Vintage Year[6]



Private credit

The long-term resilience and attractiveness of private credit has continued with the increase in rates driving higher returns across the asset class against a backdrop of relatively subdued losses. Thus far, borrowers have been able to absorb higher rates without meaningful increase in defaults thanks to continued growth in corporate earnings, borrower-friendly credit terms and strong coverage ratios prior to entering the recent rate hike cycle. As a result, private credit has increased in relative attractiveness compared to other asset classes.

[6] Source: Preqin. Fund IRR data from private equity funds as of June 30, 2023. Past performance is not a guide to future results. Future results are not guaranteed and loss of principal can occur.

Looking more closely at default rates – which spiked during the Covid-impacted 2020 – we can see they have now settled to a moderated level, currently under the average of the past three years. While they could see an uptick, it is encouraging that we have not seen a significant increase against the higher rate environment, reflecting looser covenant structures on borrowing in recent years as well as borrowers adjusting to the increased interest payments and avoiding losses.

Looking at overall market performance since 2004, the private credit asset class continues to offer an attractive risk return profile relative to large cap and public debt, as well as public equity.

Figure 9:

Private Credit Default Rates[7]

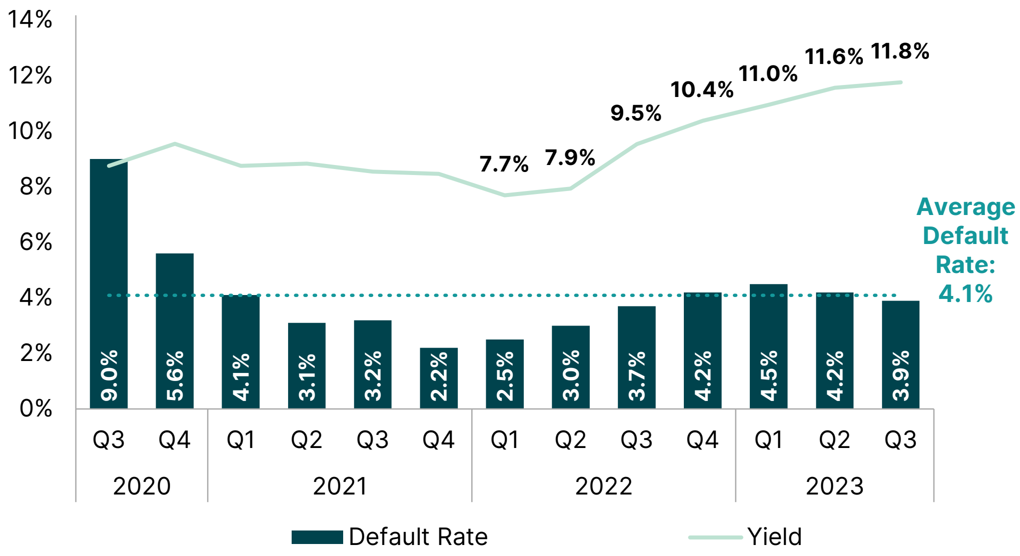
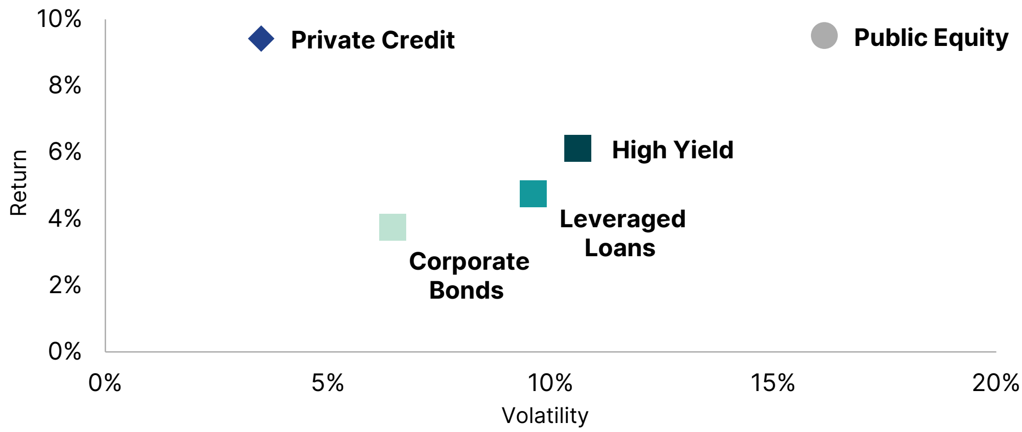


Figure 10:

Long-Term Risk Return Prolfiles[8]



[7] Source: Lincoln International and Cliffwater as of September 30, 2023. Default rates: "Q3 2023 Lincoln Senior Debt Index". Yield (current yield): "Q3 2023 Cliffwater Direct Lending Index".

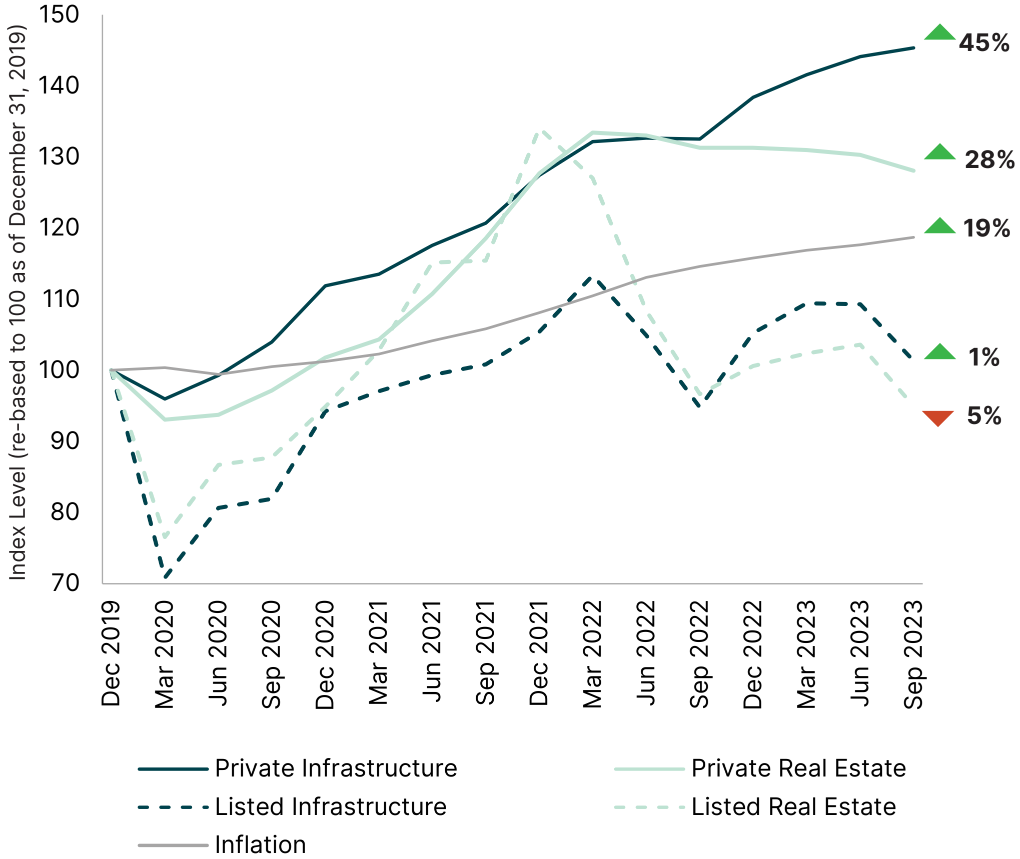
[8] Source: Cliffwater (Private Debt: Cliffwater Direct Lending Index), LCD / PitchBook (Leveraged Loans: Morningstar LSTA US Leveraged Loan Index) and Refinitiv (High Yield: ICE BofA US High Yield Index; Corporate Bonds: ICE BofA US Corporate index; Public Equity: S&P 500), as of September 30, 2023. Returns and volatility are long-term annualized figures using quarterly index data from Q4 2004 to Q3 2023. Past performance is not a guide to future results. Future results are not guaranteed and loss of principal can occur.

Real assets

Private infrastructure and real estate have exhibited insulation from increased inflation and, in the case of infrastructure, from rates. In addition, these asset classes have shown enhanced downside protection from macro volatility and outperformance of their listed market equivalents.

In the chart below, we show private infrastructure and real estate performance since December 2019, pre-Covid, compared against both inflation and listed equivalents. The clear distinction highlighted is the strong performance of private real assets relative to inflation over the period, even despite recent rates-induced falls in real estate, while public real assets, influenced by wider market trends, have failed to keep pace with price rises.

Figure 11:
Unlisted and Listed Real Assets Performance[9]



[9] Source: Cambridge Associates (Private Infrastructure; Private Real Estate), Refintiv (Listed Infrastructure: S&P Global Infrastructure; Listed Real Estate: FTSE NAREIT All Equity REITs; Inflation: US CPI) as of September 30, 2023. Past performance is not a guide to future results. Future results are not guaranteed and loss of principal can occur.

Theme 2: Potential for dealmaking to be unlocked

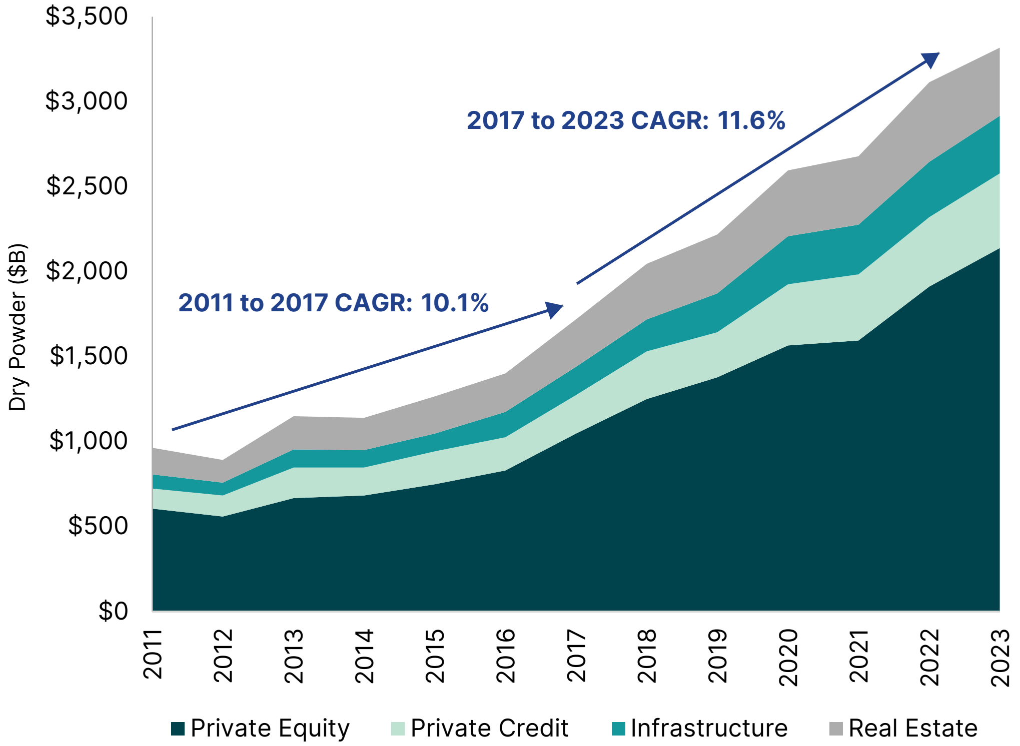
A potential resurgence in deal flow across a spectrum of asset classes could be on the horizon. The convergence of factors, from record levels of dry powder to recalibrations in pricing expectations, positions private markets for a renewed phase of dealmaking. Although some uncertainty remains, recent stabilization in deal numbers and loan volumes, coupled with a gradual decline in entry values for private equity deals, indicate a positive start to 2024.

Dry powder

The build-up of dry powder has reached record levels. In aggregate, the level of dry powder is 250% higher than it was in 2010, and almost 50% higher than it was only four years ago, now sitting at $3.3tn.[10] This reflects the broad, growing pressure in the industry for managers to put more capital to work.

Figure 12:
Dry Powder in Private Markets[10]

Record levels of dry powder have accrued, up almost 50% in only four years, resulting in an increased need to put capital to work



[10] Source: Preqin as of December 31, 2023. Private Equity includes venture capital. Secondaries and fund of fund strategies have been excluded due to double-counting.

Deal flow and valuations

Deal flow has slowed from the historical highs of Q1 2022, but activity stabilized in the second half of 2023, with a slight uptick in Q3 to levels last seen 12 months earlier. Meanwhile, deal valuations have decreased from post-Covid peaks, reflecting a reduction in pricing expectations from sellers as they adjust to an environment in which financing is less available and more expensive, and cost of capital is consequently increased. The median EV/EBITDA entry multiple has consistently fallen over the last 2 years, from 13.3x in 2021 to 10.9x in 2023, while equity contributions have stayed consistently well above 50% since 2021 and increased year-on-year in 2023.[12]

Figure 13:
Deal Activity in Private Markets[11]

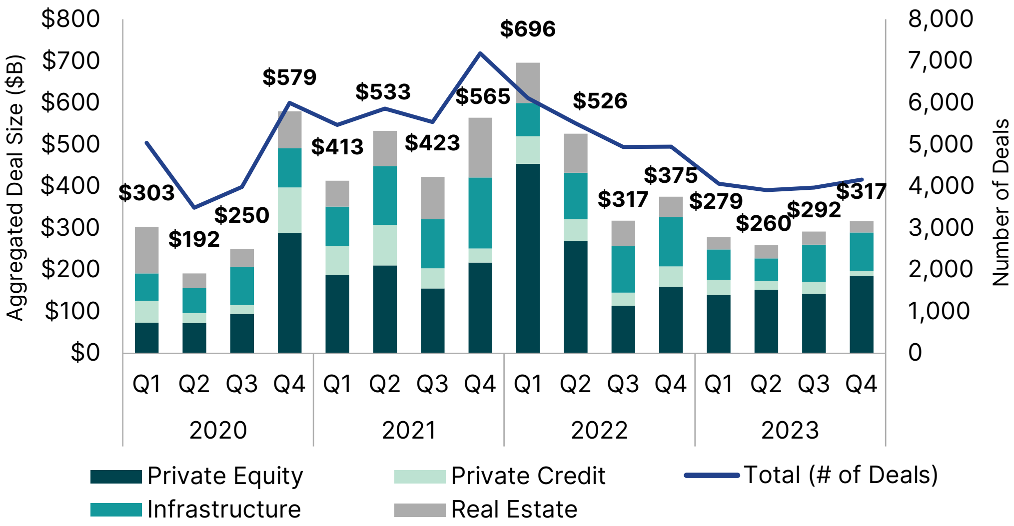
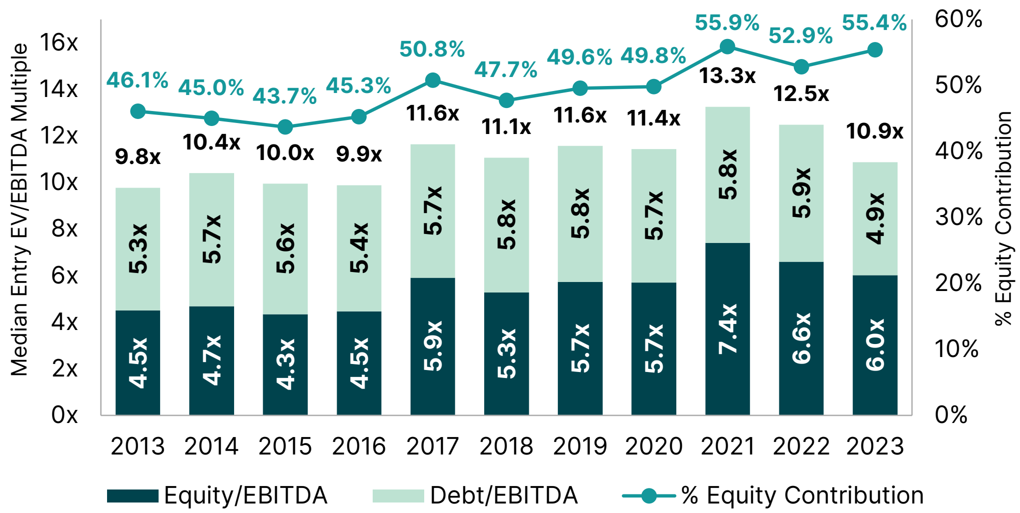


Figure 14:
Private Equity Deal Entry Multiples[12]

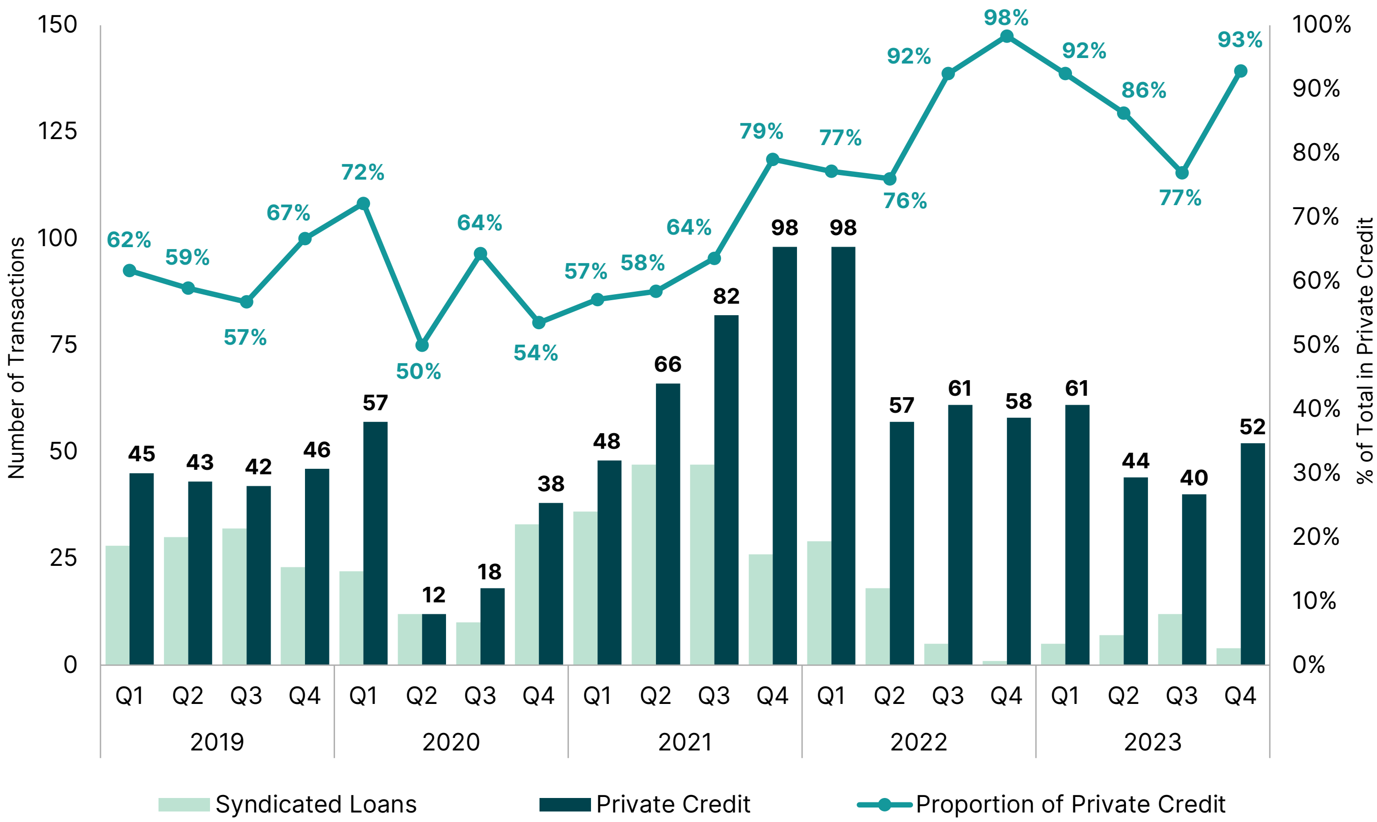


[11] Source: Preqin as of December 31, 2023.
[12] Source: PitchBook as of December 31, 2023. "2023 Annual PE Breakdown" includes private equity deals from North America and Europe.

Debt financing

With uncertain market conditions, there has been a pullback by lenders and a drop-off in LBO financing. As the market stabilizes around the higher rate regime, we expect that seasoned investors are becoming more acclimatized and cognizant of current investing conditions, subsequently leading to a predicted pick up in M&A and LBO activity. One important trend is the increased market share of private credit compared to bank lending and syndicated loans. Private credit offers more attractive terms for borrowers and increased yield for lenders. As we see an uptick in dealmaking, this should increase volumes in private credit, especially given the increasing prominence and investor interest the asset class is attracting.

Figure 15:
Leveraged Buyout Loan Volumes[13]



[13] Source: PitchBook / LCD as of December 31, 2023. Count of LBO transactions covered by LCD News.

Theme 3:
Compelling secondary opportunities

Our third theme focuses on liquidity, why we see ongoing pressure for it, how we think this can present itself and the role that secondaries markets can play in providing it.

Following the trend of 2023, the secondary market emerges as a strategic portfolio necessity in 2024, with its significance underscored by persistent liquidity demands, prolonged hold periods for private equity-backed deals, and subdued exit activity. Together, these factors spotlight the necessity for alternative liquidity routes. Secondary markets, projected to play a pivotal role in liquidity generation, offer investors avenues to navigate an evolving financial terrain.

Secondary market growth

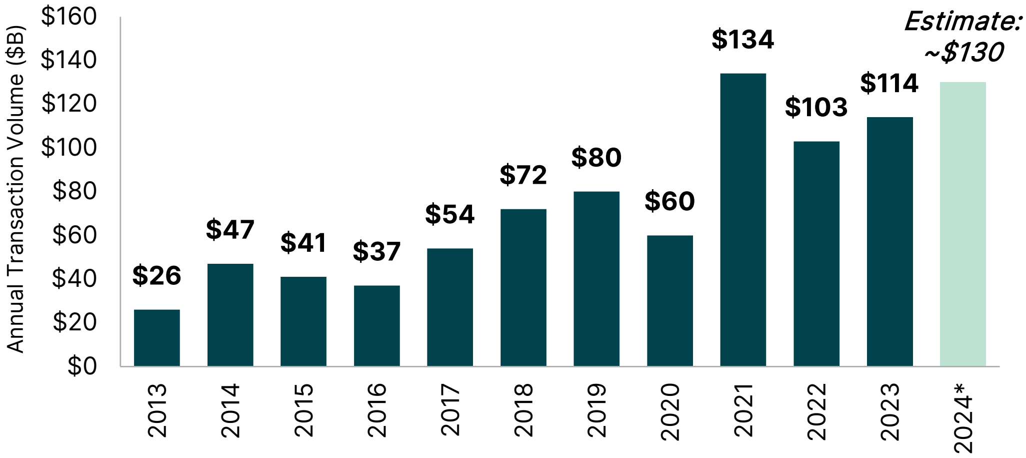
The secondaries market has grown dramatically over the last several years and is forecast to continue to build on three years of $100bn+ annual transaction volume in 2024, potentially to near-record levels. Looking into the detail, 2023 saw a slightly quieter start to the year, with $42bn in transactions completed in H1, while H2 saw a significant upswing in momentum as pricing stabilized, with $73bn in deals closed.[14]

Robust market activity is also reflected in the record amount of AUM in private equity secondaries, accounting for a growing share of the overall private equity market.

This means that a growing percentage of capital is being allocated to secondaries funds as investors identify the market's potential, which we believe will also become increasingly prevalent across the other asset classes.

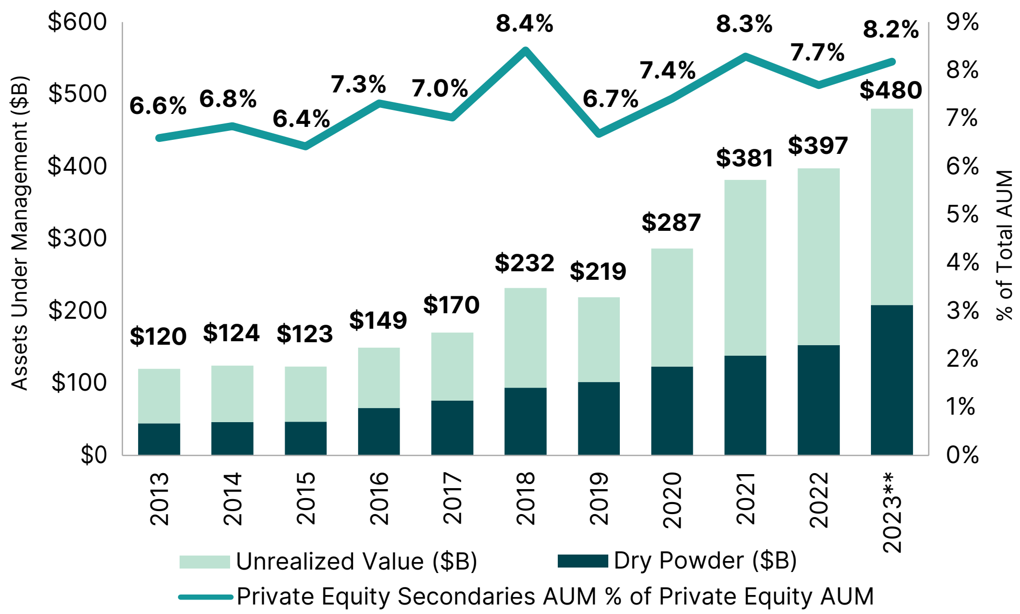
Finally, the push for liquidity may impact the discounts and valuations on secondaries investments. With more interest in the secondaries market, and more investors looking for cash, pricing may be more attractive, in turn, driving transaction volumes.

Figure 16:
Secondaries Transaction Volumes[14]



[14] Evercore and Cambridge Associates as of December 2023. 2013 to 2023 sourced from Evercore's "FY 2023 Secondary Market Survey". *2024 figure refers to a forecast from Cambridge Associates "2024 Outlook: Private Equity & Venture Capital". There is no guarantee forecasts will be realized.

Figure 17:
Secondaries Assets Under Management[15]

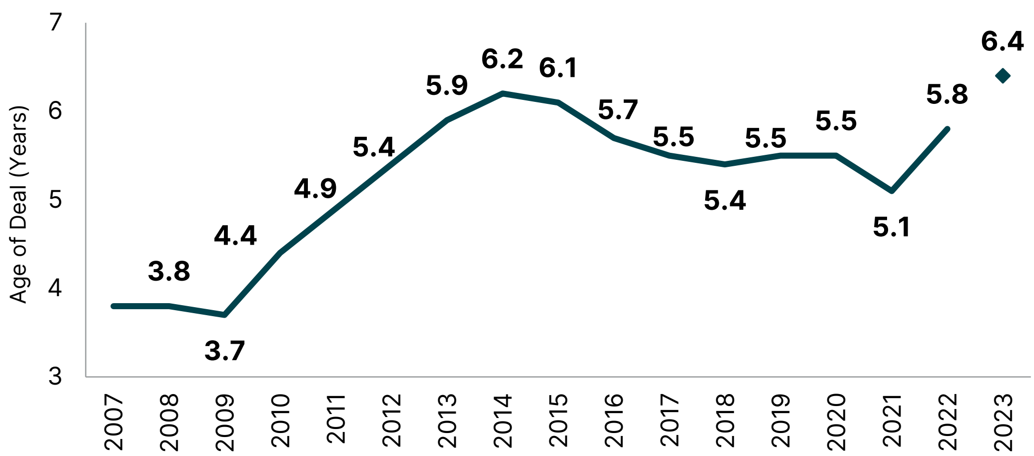


Exit activity and distributions

The average hold period for buyouts was near its highest level for more than 15 years in 2023 at 6.4 years, well above the average level since 2000 of 5.2 years.[16] Investors' extended holding periods reflect that liquidity routes have narrowed over the last couple of years, with the IPO market experiencing muted volumes and M&A transactions down considerably.

In turn, investors have been holding out for better prices, but as holding valuations become crystallized and pressure for liquidity, for example to provide capital for new fund investments, intensifies, investors will begin to look for creative solutions for their aging company inventory.

Figure 18:
Median Age of Buyout Deals at Exit[16]

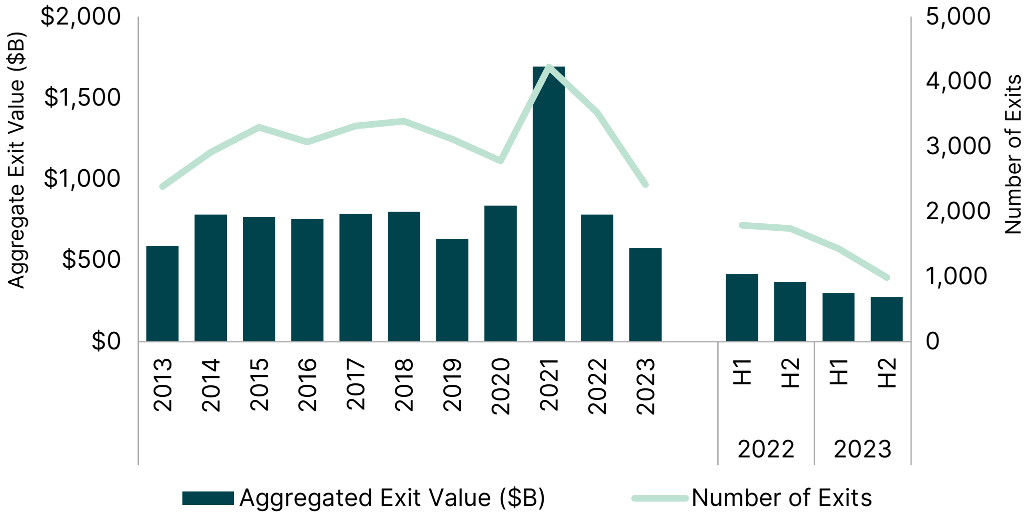


[15] Preqin as of June 30, 2023. "Secondaries" includes private equity secondaries. **2023 includes data as of Q2 2023.

[16] PitchBook as of November 11, 2023 '2024 US Private Equity Outlook'. Includes private equity buyout deals from the US.

Figure 19:

Global Buyout Exit Activity[17]



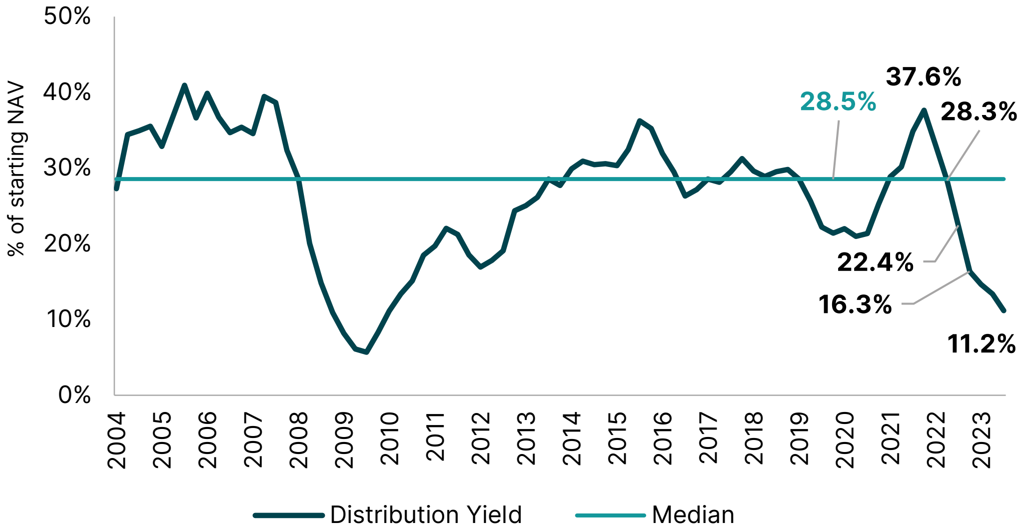
The impact of longer holding periods and low exit activity on investors is shown starkly by figures on private equity fund distributions. Distributions as a percentage of starting net asset values (NAV) for buyout funds was at its lowest since 2009 last year, and significantly below the long-term average. Moreover, with distributions from starting NAV standing at close to 11%, all things remaining equal it would take 9-10 years to return value currently held in buyout funds, highlighting the need for investors to realize capital to fund new allocations.

The pressure for liquidity generation from fund investors will continue to mount, helping to narrow buyer and seller price disparity and boost transaction volumes in the secondaries markets.

Figure 20:

Trailing 12-Month Buyout Fund Distributions as a % of starting NAV[18]

Distribution yields are falling, currently at the lowest levels since the GFC as GPs are having difficulty returning capital to LPs.



[17] PitchBook as of December 31, 2023. Includes global private equity buyout exits.

[18] Source: Pitchbook as of September 30, 2023 '2024 Allocator Outlook'. Includes private equity buyout funds from the US. Data for the two most recent quarters was estimated based on exit value.

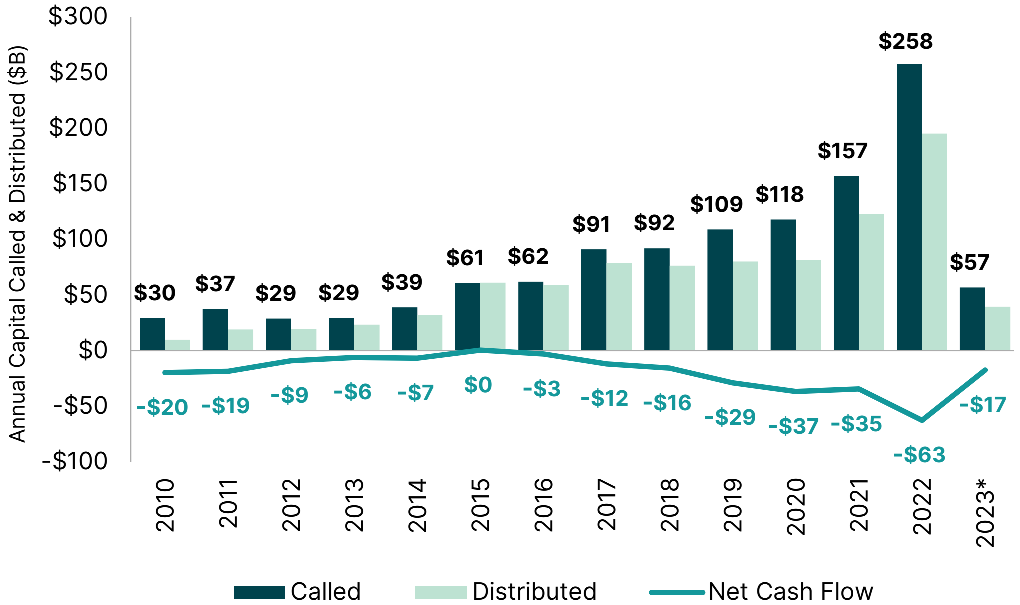
Real assets perspective

Investors across real assets are in search of liquidity and capital solutions, supporting the continued innovation as well as the widening adoption across asset classes in the secondaries market. In the infrastructure market, the trend of reduced distributions also holds true, with calls continuing to outstrip distributions. This should continue to support the growth of secondaries solutions.

Turning to real estate and looking at the level of debt due to mature in the next five years, there is a rising tide of maturities due. The level of commercial real estate loans maturing between 2024 – 2028 is forecast to increase to an annual average of $561bn, giving a total of $2.8tn maturing in the next five years. This represents a 39% increase from the $400bn average seen between 2020-2022[19]. Property values have also come under pressure, which, combined with a 22-year high Fed base rate, will likely create challenges for lenders and borrowers alike in rolling such a high volume of maturing debt. Naturally, this should increase demand for capital solutions.

Figure 21:
Infrastructure Capital Calls & Distributions[20]

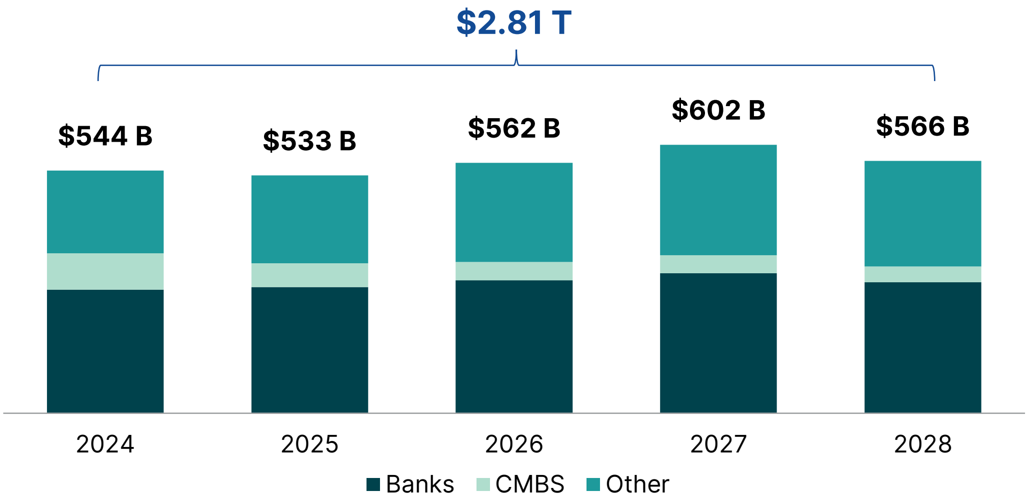
Capital calls in infrastructure funds reached an all-time high in 2022



[19] Trepp and Federal Reserve as of November 2023. “Other” includes government-sponsored entities, pension plans, insurance companies, and finance companies.

[20] Source: Preqin as of September 30, 2023. Aggregated annual capital flows for global unlisted infrastructure funds. *2023 includes data from Q1 to Q3 2023.

Figure 22:
Commercial Real Estate Loan Maturity[21]



Conclusion

The economy is more settled than it was this time last year, but uncertainty remains, and interest rates are expected to remain higher for longer. Financing market pressures will continue, but private markets have shown resilience and there is increased focus on manager and thematic selection as returns dispersion has widened. Recent stabilization, moderation in new deal values, and high levels of dry powder to put to work, create the potential for dealmaking to be unlocked. Opportunities in the secondary market remain compelling and 2024 could see record deal levels, as liquidity needs remain heightened due to slower exits and distributions.

Pantheon's steadfast commitment to a disciplined, high-conviction investment approach, coupled with our strong positioning across private market secondaries, where we have a 36-year investment track record, positions us as valuable guides through this intricate landscape. As investors navigate the complexities across diverse asset classes, a keen understanding of these key themes becomes paramount for success in the dynamic world of private markets.

[21] Trepp and Federal Reserve as of November 2023. "Other" includes government-sponsored entities, pension plans, insurance companies, and finance companies. The forecasts highlighted are for information purposes only. There is no guarantee these forecasts will materialize.

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