eFront Quarterly Report

PRIVATE EQUITY PERFORMANCE OVERVIEW

Returns, risks and liquidity of VC Funds in Q3 2020

eFront
a part of BlackRock

Introduction

eFront is the leading provider of alternative investment technology, focused on enabling industry professionals to achieve superior performance. This report leverages high quality data and powerful analytics coming from eFront Insight. eFront Insight combines multiple data sources into one analytical platform. It includes a proprietary benchmark for alternative investment performance, counting over 4,000 funds across geographies, strategies, sizes and vintage years. This is the main data source of this report. On a quarterly basis, eFront publishes an updated report showing the performance of LBO and VC funds in terms of returns, risks and liquidity. The performance of LBO and VC funds are analyzed in a sequence one quarter after the other.

The aim of this report is to provide readers with elements of analysis and understanding of the private finance universe, based only on data collected by eFront Insight. It does not intend to draw any definitive conclusion, nor judge the performance of fund managers. By providing a guided reasoning, this report hopes to contribute to the overall progress of understanding of the asset class in a short quarterly format, with all the limits that this entails.

Contents

1. GLOBAL MARKET PERFORMANCE OVERVIEW

Return analysis
Risk analysis
Liquidity analysis

2. VINTAGE YEAR & REGIONAL PERFORMANCE OVERVIEW

General evolution
US VC funds
Western European VC funds

METHODOLOGY

Global Market Performance Overview

SUMMARY OF THE ANALYSIS

Performance has reached a plateau, above 1.6x, away from the pandemic challenges. Meanwhile, the selection risk has increased, potentially charting a new course for active VC funds, with more differentiation among fund managers. Distributions remain robust as the time-to-liquidity is fairly stable at 3.5 years.

Active VC funds have so far weathered the pandemic storm. Performance is at an all-time high, but so is the selection risk.

PERFORMANCE ANALYSIS (FIG. 1 AND 2)

It is difficult to find any impact of the current pandemic on the performance of active VC funds. Their aggregated multiple of invested capital (TVPI) reached an all-time high of 1.64x in Q2 2020 when the pandemic was unfolding (Fig. 1). The performance has now reached a plateau above the 1.6x threshold, hovering from 1.58x to 1.64x during the last four quarters. This is a far cry from a correction.

The first three quarters of 2020 show an even higher positive deviation from the average TVPI (Fig. 2) than in 2019, which was already an exceptional year. Therefore, in terms of performance, active VC funds have so far gone from record to record. This evolution echoes the progression of the valuation of listed technological companies.

FIG. 1 – RETURN EVOLUTION OF ACTIVE VC FUNDS

Source: eFront Insight, As of Q3, 2020

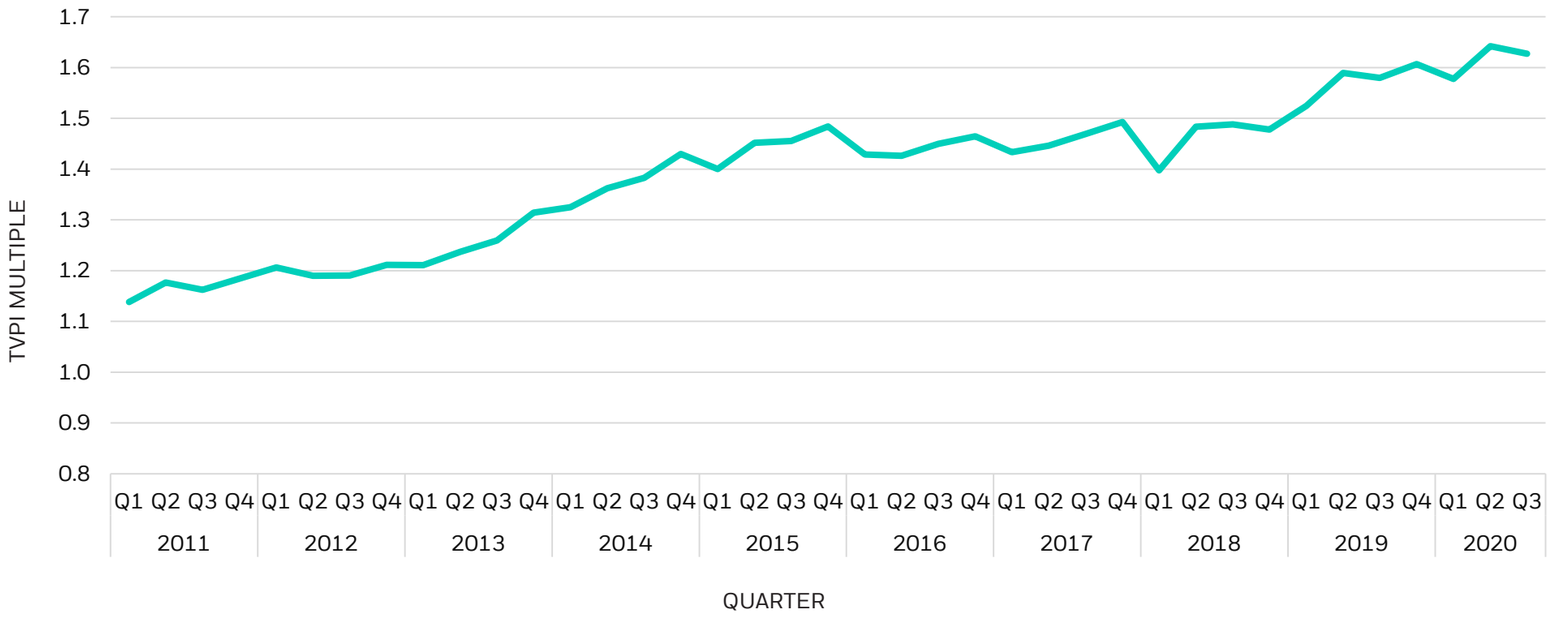
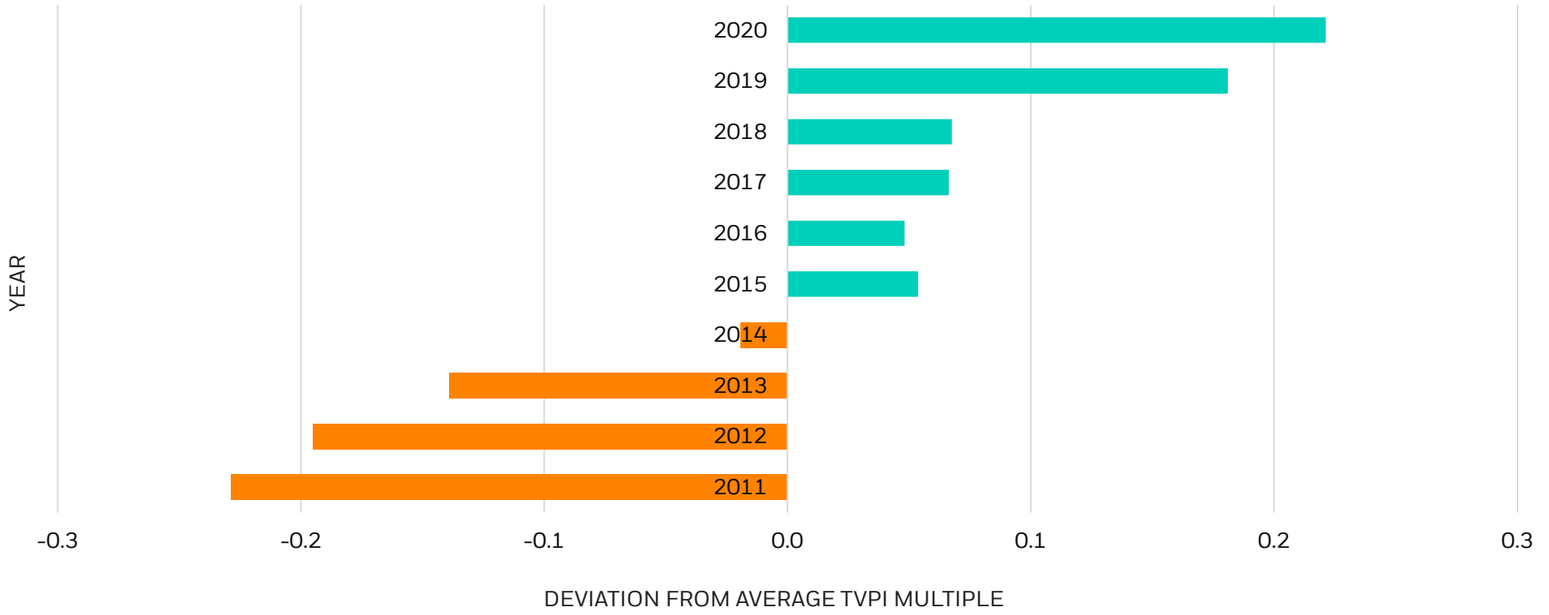


FIG. 2 – RETURN DEVIATION FROM THE AVERAGE OF ACTIVE VC FUNDS

Source: eFront Insight, as of Q3 2020. Basis 0 = net average of 1.38x



RISK ANALYSIS (FIG. 3 AND 4)

The difference of performance between fund managers belonging to the top and the bottom 5% (TVPI spread) has increased to the levels last seen in Q2 and Q3 2019 (Fig. 3). Q2 2020 set a new record at 1.98x. Therefore, the selection of VC fund managers is very demanding. The TVPI spread might even cross the 2.0x threshold. Currently, the top 5% reaches a performance of 2.75x, while the bottom records a 0.79x, resulting in the manager performance spread of 1.96x.

Thus, in terms of TVPI spread, the first three quarters of 2020 have deviated the most from the average of active funds (Fig. 4). Until recently, the performance was essentially increasing (from 1.3x in 2014 to 1.6x now) while the risk remained fairly stable (in the range 1.5x to 2.0x). The fact that the TVPI has stabilised while the TVPI spread has increased is somewhat new. This divergence from historical patterns could be a short-term phenomenon or the early sign of a deeper trend.

Indeed, it could signal more challenging market conditions, in which some managers thrive, while others increasingly struggle. It could also mark the end of a cycle. However, this evolution would need to be confirmed over multiple successive quarters to draw definitive conclusions.

FIG. 3 – RISK EVOLUTION OF ACTIVE VC FUNDS

Source: eFront Insight, As of Q3, 2020

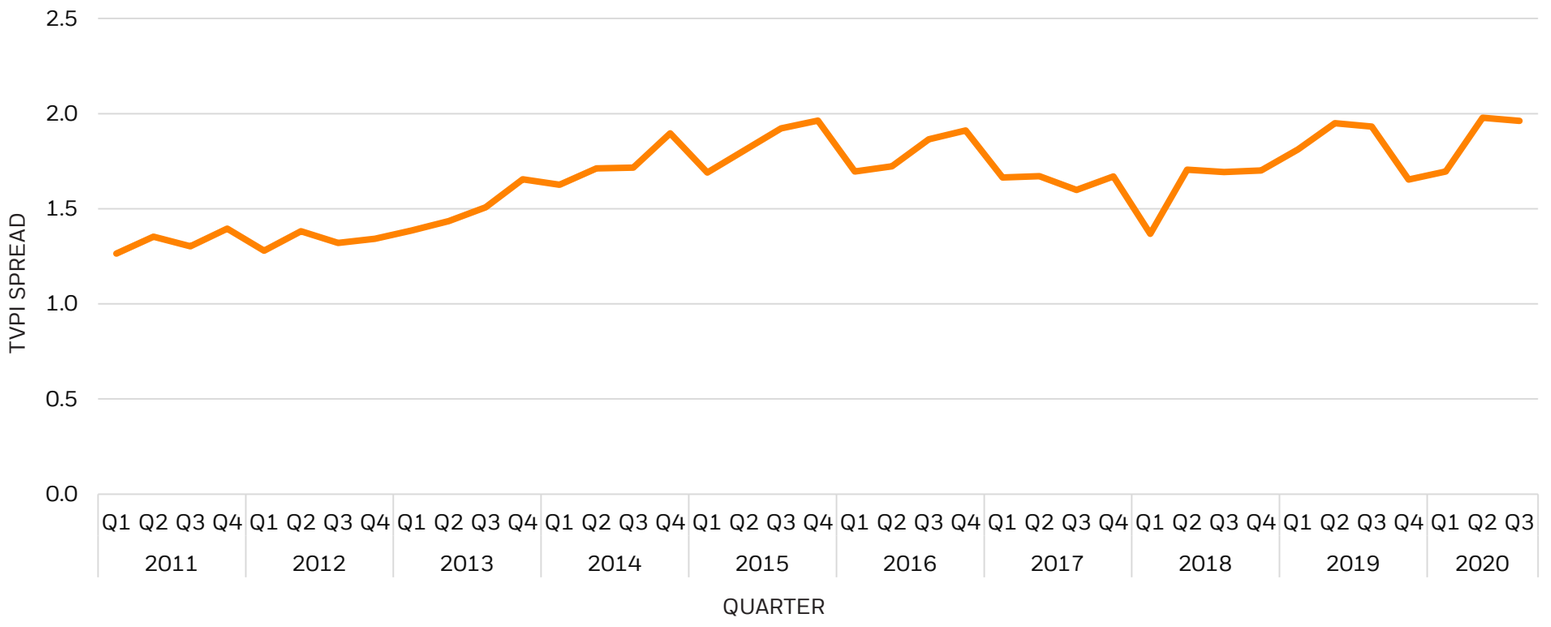
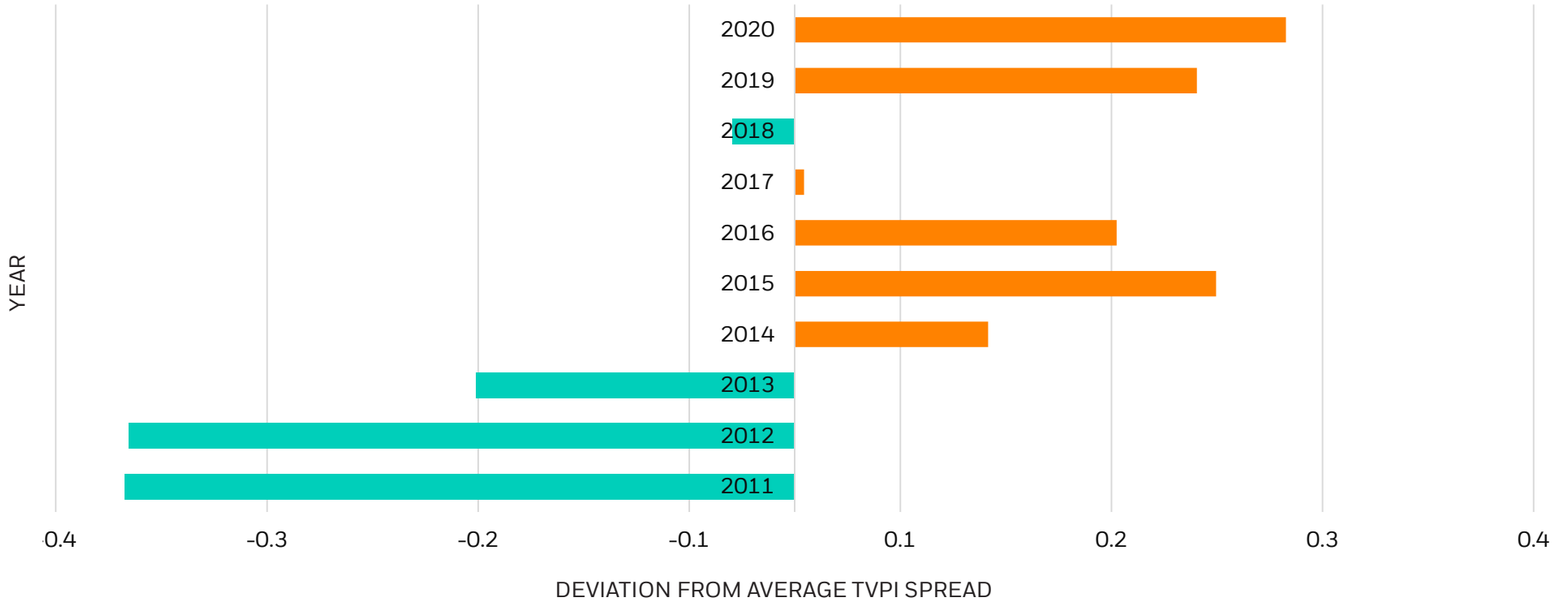


FIG. 4 – RISK DEVIATION FROM THE AVERAGE OF ACTIVE VC FUNDS

Source: eFront Insight, as of Q3 2020. Basis 0 = average of 1.63x.



LIQUIDITY ANALYSIS (FIG. 5 AND 6)

The time-to-liquidity is remarkably stable since Q2 2019 (Fig. 5). On average investors receive capital back after 3.48 years. This is slightly above the average of active funds, standing at 3.33 years (Fig. 6). This implies that the peak of TVPI highlighted above is a mix of distributions and increase of net asset values.

These distributions are good news for fund investors and managers alike. For the former, this is a reassuring perspective on valuations and performance. For the latter, this ensures that investors have capital for upcoming fundraising exercises. Track records matching with distributions are a solid argument in a competitive fundraising environment.

FIG. 5 – LIQUIDITY EVOLUTION OF ACTIVE VC FUNDS

Source: eFront Insight, As of Q3, 2020

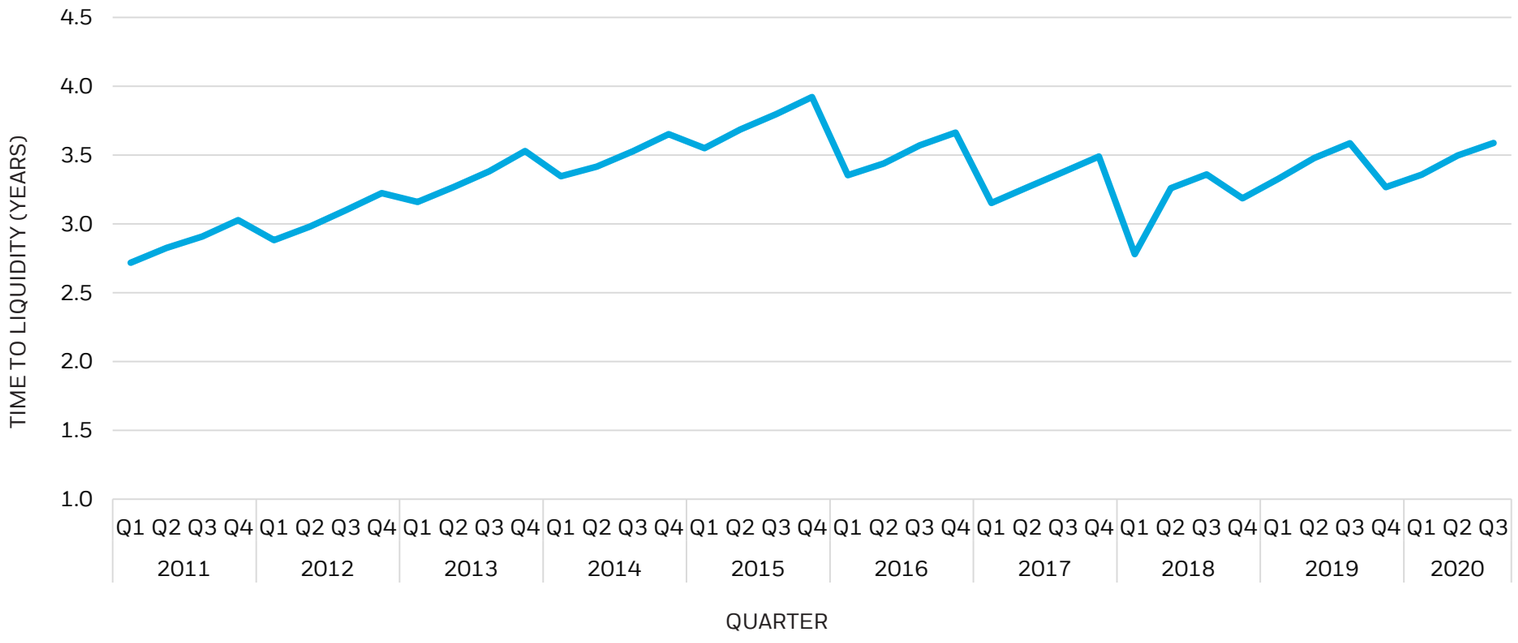
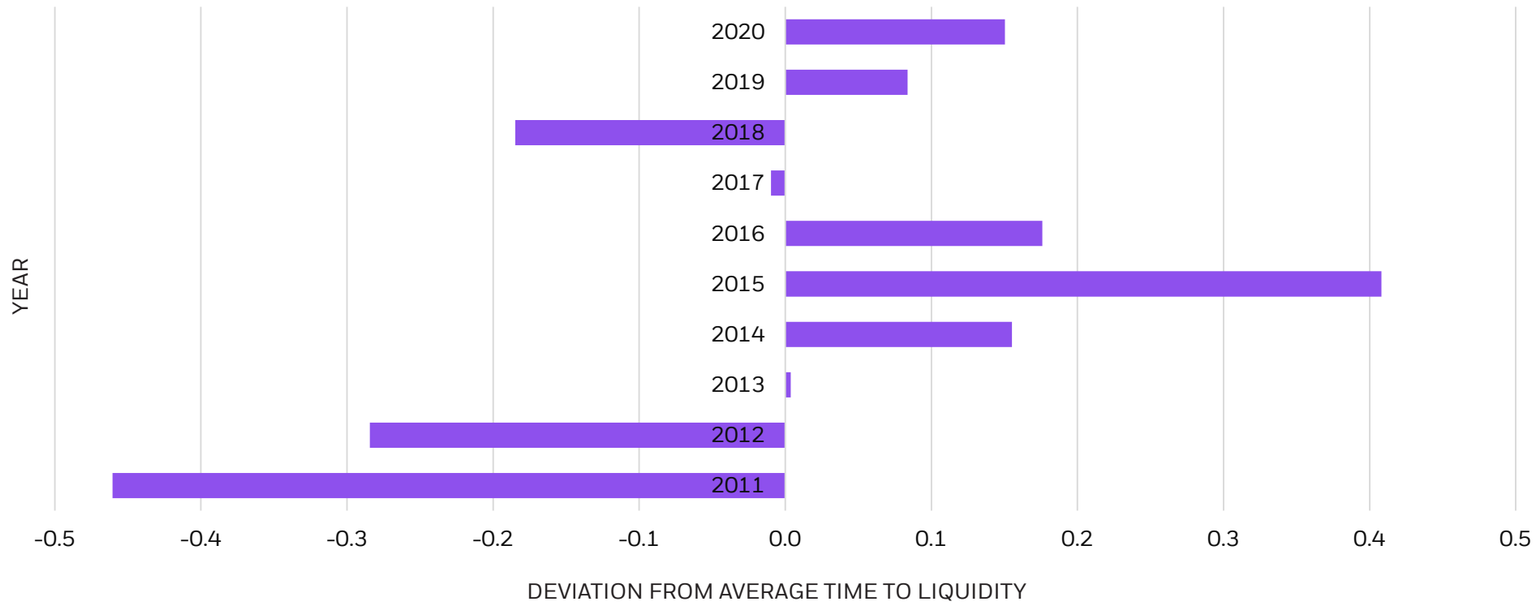


FIG. 6 – LIQUIDITY DEVIATION FROM THE AVERAGE OF ACTIVE VC FUNDS

Source: eFront Insight, as of Q3 2020. Basis 0 = average holding period of 3.33 years.



Vintage Year & Regional Performance Overview

SUMMARY OF THE ANALYSIS

American VC funds have recorded a correction in Q1, followed by a rebound and a stabilization of their TVPI. Their European peers evolved more moderately but recorded a decline of their multiples in Q3 2020.

Active VC funds have seen their TVPI stabilize. As a consequence, majority of vintage years remained around the historical average, while the strong ones continue to outperform it.

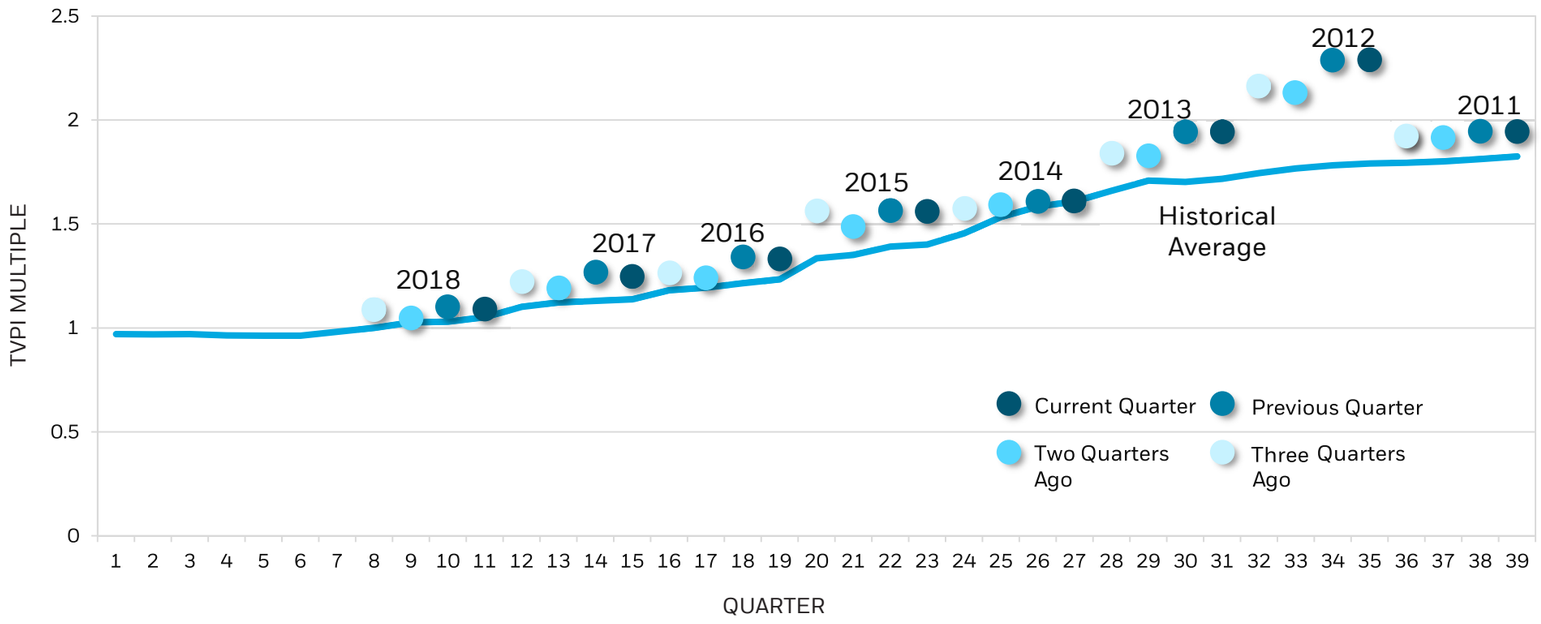
GENERAL EVOLUTION (FIG. 7)

Active VC funds have recorded a stabilization of their TVPI during Q2 and Q3 2020, in line with the conclusions in the previous section. Therefore, the overall picture remains essentially unchanged (Fig. 7).

Individual vintage years stayed on course, which had two consequences. First, vintage years that were close to the average (2014 and 2016) kept their positions. The strong ones (2011,2012, 2013 and 2015) continue to fare well, although 2015 seems to be on the course towards the historical average.

FIG. 7 – EVOLUTION OF MULTIPLES OF ACTIVE GLOBAL VC FUNDS

Source: eFront Insight, as of Q3 2020. Active funds grouped by vintage year. The current average includes only fully realized funds to 2010. Reference currency: USD.

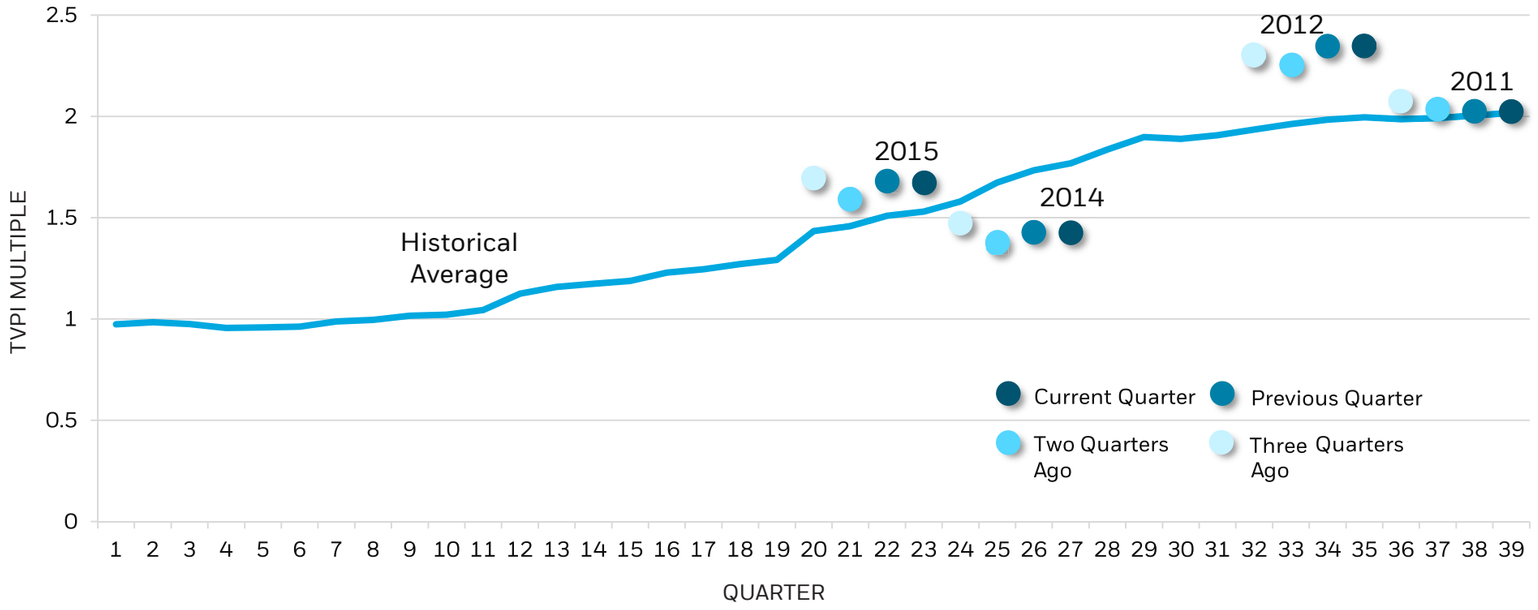


US VC FUNDS (FIG. 8)

Active US VC funds have recorded a decrease in their multiples of invested capital in Q1 2020. Q2 lead to a rebound and Q3 a stabilisation (Fig. 8). This evolution seems to mimic, to a certain extent, those of the price of listed stocks of American technological companies.

FIG. 8 – EVOLUTION OF MULTIPLES OF US VC FUNDS

Source: eFront Insight, as of Q3 2020. Active funds grouped by vintage year. The current average includes only fully realized funds to 2010. No data for 2013 and 2016. Reference currency: USD.



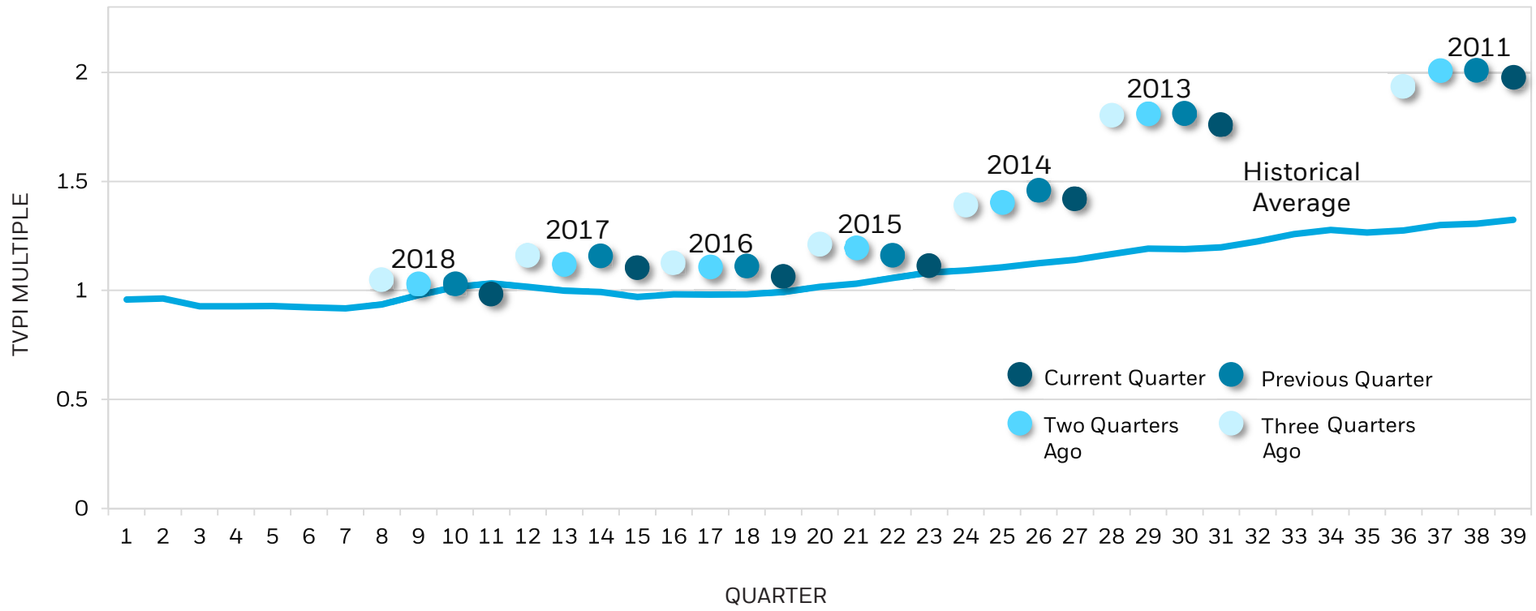
WESTERN EUROPEAN VC FUNDS (FIG. 9)

In general, WE VC funds have recorded a decline of their multiples of investment in Q3 2020 (Fig. 9). Q2 2020 has been more contrasted, ranging from an increase (vintage years 2014 and 2016), a stabilisation (2011 and 2013), to a decline (2015).

Despite a decline of its TVPI, the vintage year 2013 continues to outperform the historical average. As 2011 will leave the sample, it will be integrated into the average. This will contribute to lifting it, as the performance is particularly high. As a consequence, some of the recent vintage years might cross the historical average and underperform it.

FIG. 9 - EVOLUTION OF MULTIPLES OF W. EUROPEAN VC FUNDS

Source: eFront Insight, as of Q3 2020. Active funds grouped by vintage year. The current average includes only fully realized funds to 2010. Reference currency: EUR.



METHODOLOGY

Global Overview

Fig. 1 is based on multiples of invested capital (total value to paid-in, TVPI), the sum of capital distributed (distributed to paid-in, DPI) and net asset values (residual value to paid-in, RVPI). The purpose is to exhibit the evolution over time of valuations of active funds only, to get a perspective on performance in the making. Each quarter, a snapshot of the pooled average TVPI of active funds is taken. These funds are active (thus not older than 10 years old) with meaningful performance (thus not younger than two years old). In 2010, active vintage years are from 2001 to 2008. In 2011, active vintage years are from 2002 to 2009. The purpose is to track the evolution of active portfolios and their maturity to compare them over time.

Fig. 2 compares quarterly deviations of TVPIs of active funds from the historical average of TVPIs of active funds (as a base 0). The purpose is to exhibit evolutions over time when compared to a long-term reference point. Except for the quarter considered (or full year when considering Q4), historical deviations are grouped per year (thus the snapshots taken in Q1, Q2, Q3, Q4 2010 are grouped as an average under “2010”). If TVPIs are above average, they exhibit a relative excess of performance during the period considered. If TVPIs are below average, they exhibit a relative lack of performance during the period considered.

Fig. 3 is based on the difference between top 5% and bottom 5% TVPI (TVPI spread), which is used as a measure of VC fund selection risk. The resulting graph shows a quarterly evolution. The purpose is to exhibit the evolution over time of the dispersion of performance of the best and worst fund managers. Each quarter, a snapshot of the TVPI spread of active funds is taken. These funds are active (thus not older than 10 years old) with meaningful performance (thus not younger than two years old). In 2010, active vintage years are from 2001 to 2008. In 2011, active vintage years are from 2002 to 2009. The purpose is to track the evolution of active portfolios and their maturity to compare them over time.

Fig. 4 compares quarterly deviations of TVPI spreads of active funds from the historical average of TVPI spreads of active funds (as a base 0). The purpose is to see evolutions over time when compared to a long-term reference point. Except for the quarter considered (or full year when considering Q4), historical deviations are grouped per year (thus the snapshots taken in Q1, Q2, Q3, Q4 2010 are grouped as an average under “2010”). If TVPI spreads are above average, they exhibit a relative excess of risk during the period considered. If TVPIs are below average, they exhibit a relative lack of risk during the period considered.

Fig. 5 is based on the calculated time-to-liquidity (measured as a function of TVPI and IRR, to extract the time necessary to achieve the second from the first). The purpose is to exhibit the evolution over time of the time necessary to generate liquidity, whether through exits, dividend recaps, but also write-offs. This measure is theoretical and sensitive to the assumption that portfolios are considered as liquid during the quarter in which the snapshot is taken. Each quarter, a snapshot of the pooled average TVPI and IRR of active funds is taken. These funds are active (thus not older than 10 years old) with meaningful performance (thus not younger than two years old). In 2010, active vintage years are from 2001 to 2008. In 2011, active vintage years are from 2002 to 2009. The purpose is to track the evolution of active portfolios and their maturity to compare them over time.

Fig. 6 compares quarterly deviations of time-to-liquidity (measured in years) of active funds from the historical time-to-liquidity of active funds. The purpose is to exhibit evolutions over time when compared to a long-term reference point. Except for the quarter considered (or full year when considering Q4), historical deviations are grouped per year (thus the snapshots taken in Q1, Q2, Q3, Q4 2010 are grouped as an average under “2010”). If the time-to-liquidity falls below 2.5 years or exceeds 4 years, it is considered sub-optimal. In the case of a time-to-liquidity shorter than 2.5 years, fund managers do not have the time to maximize their performance. In the case of a time-to-liquidity above 4 years, fund managers struggle to exit or refinance their assets and might have difficulties to maximize performance.

Vintage Year and Regional Overview

This analysis is based on the fact that private equity funds follow a certain course from inception to their liquidation. To shed a light on the funds currently active, we plot their pooled average TVPI during the current and past three quarters. These funds are aggregated by vintage year. TVPIs provide a perspective on realized and unrealized returns. TVPIs of active funds at a certain stage of their development can usefully be compared with the TVPIs of fully realized funds at the same stage of their development. The latter ones are materialized by the continuous blue line on the graphs and aggregated funds fully realized funds of vintage year up to 2010.

How eFront Insight can help LPs manage their private market programs

This paper was produced using eFront Insight which offers data services that collect and validate cash-flows from thousands of unique funds that are then used on an anonymized basis to generate net return calculations and provide an Industry benchmark.

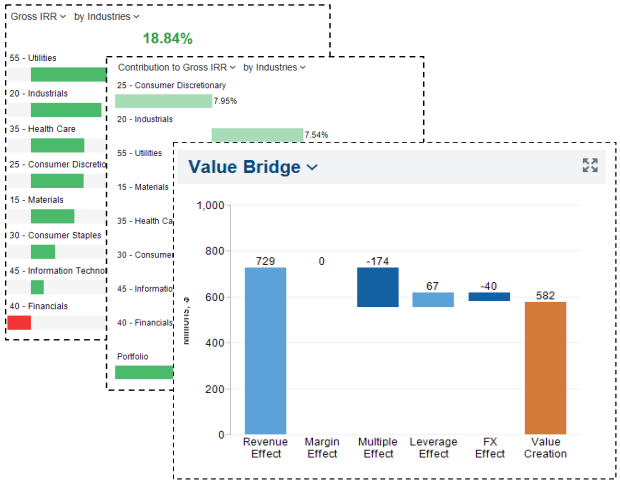
Additionally, eFront Insight provides Limited Partners with a rich data set relating to their portfolio funds and underlying holdings, sourced directly from General Partners and enriched with 3rd party feeds including Public indices, and media sources.

This data set can be interrogated via eFront Insights powerful UI consisting of out of the box analytics, configurable tear sheets, and API interoperability.

Limited Partners are leveraging the platform to generate superior insight regarding Private Markets as a whole, via the industry benchmark, and through unrivalled detail and transparency in relation to their performance and exposures across all investment levels.

The data and toolkit available within eFront Insight enables Investors to assess the constituents of their private market exposure, and attribute performance across multiple dimensions, enabling the assessment of drivers and effects created through changing market conditions and the private market correlations to public markets.

Company level financial data provides sophisticated value creation bridge analysis at the underlying holdings level enabling LPs to evaluate the impact of operational changes and macroeconomic events on the residual value in their portfolios.



TO LEARN MORE ABOUT EFRONT INSIGHT, **DOWNLOAD THE BROCHURE** OR **CONTACT US.**

eFront is the leading technology solution for alternative investment management, covering the needs of all alternative investment professionals end-to-end, from fundraising and portfolio construction to investment management and reporting. With more than 850 clients in 48 countries, eFront services clients worldwide across all major alternative asset classes. In 2019, eFront was acquired by BlackRock and integrated with Aladdin®, its investment technology, bringing together public and private asset classes to deliver the industry-leading multi-asset investment platform.

eFront
a part of BlackRock