2020-2021

Australian Institutional Investor Survey of Private Equity & Venture Capital Investing

Private Equity Media

Authors: Alistair McCreadie, Simon Uzcilas, Adrian Herbert

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APEX

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Executive Summary

Key findings

Average allocations up

The average allocation to private equity and venture capital planned for 2020-21 was 5.6%, up from 4.14% in 2019-20 and marginally above the 2018-19 figure of 5.55%.

No changes planned

The largest percentage of respondents (more than 55%) planned to keep allocations to the sector unchanged, or were undecided, whereas in the 2019-2020 survey the largest percentage (50%) planned to increase allocations.

Funding for new managers

Despite most respondents planning to keep their overall allocations unchanged, more than 55% said they anticipated making fresh commitments so, clearly, they are considering funding new managers.

Local market gains ground

While most respondents continued to rank the North American market as their first preference for investing in private equity and venture capital the Australia and New Zealand market was an even closer second choice compared with the previous survey.

High rates of return targeted

The net rates of return targeted for 2020-21 remained high with more than 55% of respondents targeting more than 15 per cent net of fees and more than 30% targeting listed equities plus 3%.

Value for money still high

Close to 80% of respondents considered that, on a risk adjusted basis, their private equity and venture capital investments offered value for money. This was, however, down from 90% in the previous survey.

Interest in venture capital

Interest in allocating specifically to Australian venture capital remained high although slipping from the high of the previous survey. A total of 22% of respondents expressed the highest level of interest, more than 55% reported median interest and 23% negative interest.

Interest in private equity strong

Interest in allocating to Australian private equity and venture capital remained strong with 22% of respondents highly interested, 55% expressing median interest and 22% negative interest.

Specialised investment staff down

The number of equivalent full-time professionals in respondents' private equity and venture capital teams averaged just 2.2. This was down from 3.35 in the previous survey.

Conclusions

While more than 55% of survey respondents reported they planned to keep their allocations to private equity and venture capital unchanged this was a significant change from the previous survey when 50% had planned to increase their allocations.

The previous survey was completed before the pandemic so economic uncertainty caused by COVID-19 and resulting negative economic forecasts have clearly affected confidence since then. But alterations to the superannuation system plus foreshadowed further alterations also probably changed views on the role of illiquid assets in the portfolios of super funds. Allocations to private equity and venture capital also possibly reached a cyclic high point in comparison to other asset classes in the previous survey.

Whatever the precise reasons, responses in the current survey reflected increased economic uncertainty.

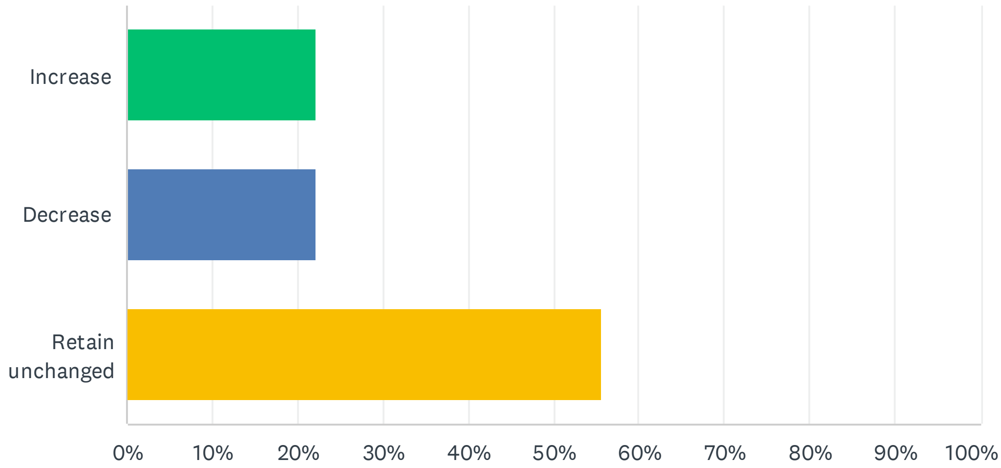
Consolidated Survey Responses

Q1. Percentage of portfolio allocated to private equity and venture capital as at 1 July 2020?

Percentage of portfolio allocated to private equity and venture capital as at 1 July 2020
5.00%
2.00%
6.50%
2.50%
14.00%
6.00%
1.85%
10.30%
2.50%
Average: 5.62%

(Answered: 9 Skipped: 0)

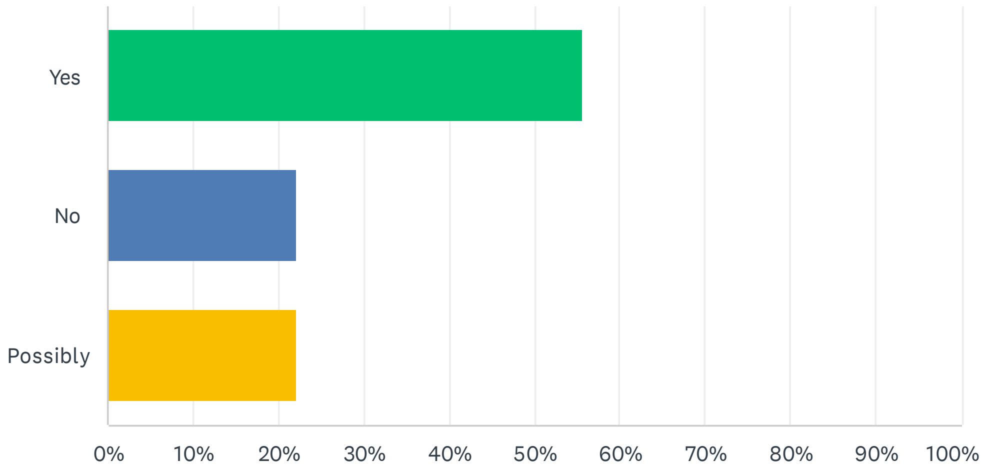
Q2. Do you plan to change your total allocation to private equity and venture capital investments over the 12 months started 1 July 2020?



Answer Choices	Responses	
Increase	22.22%	2
Decrease	22.22%	2
Retain unchanged	55.56%	5
TOTAL		9

(Answered: 9 Skipped: 0)

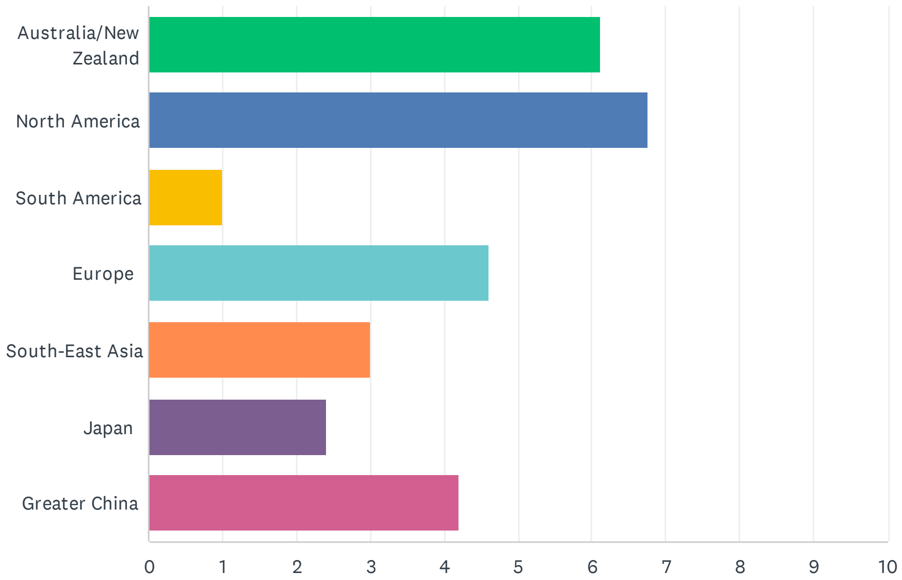
Q3. Do you anticipate making fresh commitments to private equity or venture capital investing over the 12 months started 1 July 2020?



Answer Choices	Responses	
Yes	55.56%	5
No	22.22%	2
Possibly	22.22%	2
TOTAL		9

(Answered: 9 Skipped: 0)

Q4. Rank in order the geographic regions in which you anticipate your fund will invest in private equity and venture capital over the 12 months started 1 July 2020. (1 indicating highest level of investment.)



	1	2	3	4	5	6	7	Total	Average Ranking
Australia/New Zealand	25.00% 2	62.50% 5	12.50% 1	0.00% 0	0.00% 0	0.00% 0	0.00% 0	8	6.13
North America	75.00% 6	25.00% 2	0.00% 0	0.00% 0	0.00% 0	0.00% 0	0.00% 0	8	6.75
South America	0.00% 0	0.00% 0	0.00% 0	0.00% 0	0.00% 0	0.00% 0	100.00% 5	5	1.00
Europe	0.00% 0	20.00% 1	40.00% 2	20.00% 1	20.00% 1	0.00% 0	0.00% 0	5	4.60
South-East Asia	0.00% 0	0.00% 0	0.00% 0	40.00% 2	20.00% 1	40.00% 2	0.00% 0	5	3.00
Japan	0.00% 0	0.00% 0	0.00% 0	0.00% 0	40.00% 2	60.00% 3	0.00% 0	5	2.40
Greater China	0.00% 0	0.00% 0	40.00% 2	40.00% 2	20.00% 1	0.00% 0	0.00% 0	5	4.20

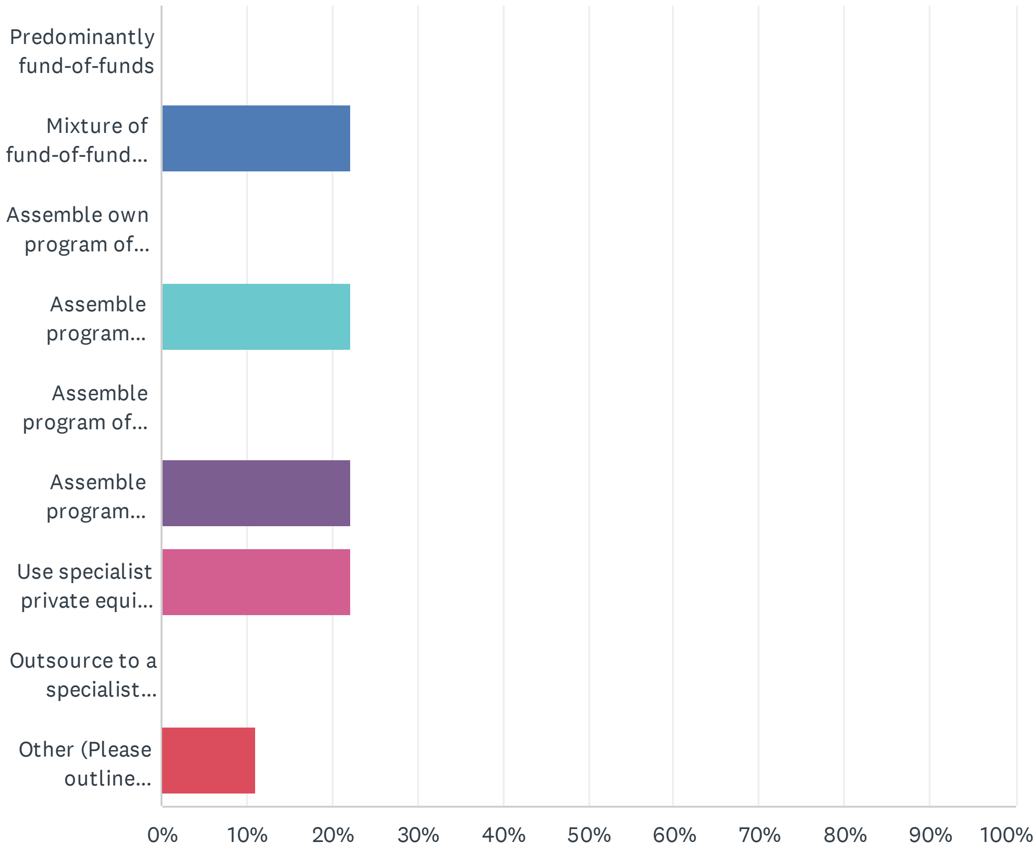
(Answered: 8 Skipped: 1)

Q5. Number of equivalent full-time professionals in your private equity and venture capital team as at July 2020?

Number of equivalent full-time professionals in your private equity and venture capital team as at July 2020
7.00
0.50
3.50
1.00
0.00
3.00
1.00
2.00
2.00
Average: 2.20

(Answered: 9 Skipped: 0)

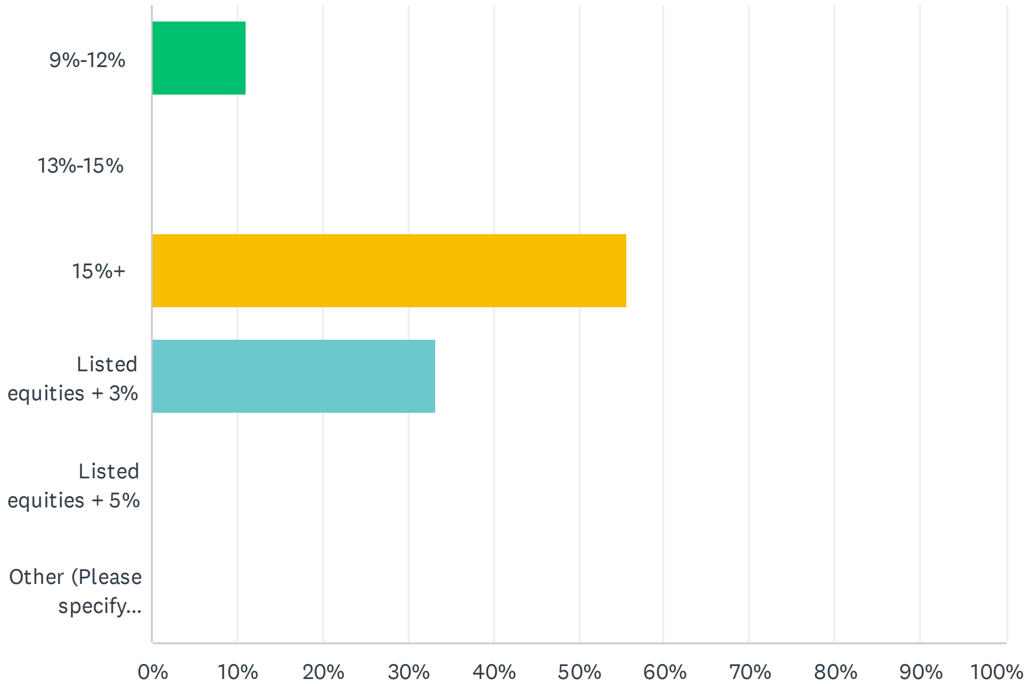
Q6. What is your preferred execution/implementation approach for your private equity and venture capital allocation?



Answer Choices	Responses	
Predominantly fund-of-funds	0.00%	0
Mixture of fund-of-funds and individual funds	22.22%	2
Assemble own program of diverse individual fund relationships	0.00%	0
Assemble program including some co-investments	22.22%	2
Assemble program of predominantly direct investments	0.00%	0
Assemble program including co-investments and direct holdings in managers' investee companies	22.22%	2
Use specialist private equity adviser for research and advice but make final investment decisions	22.22%	2
Outsource to a specialist adviser/manager to implement on discretionary basis	0.00%	0
Other (Please outline briefly)	11.11%	1
TOTAL		9

(Answered: 9 Skipped: 0)

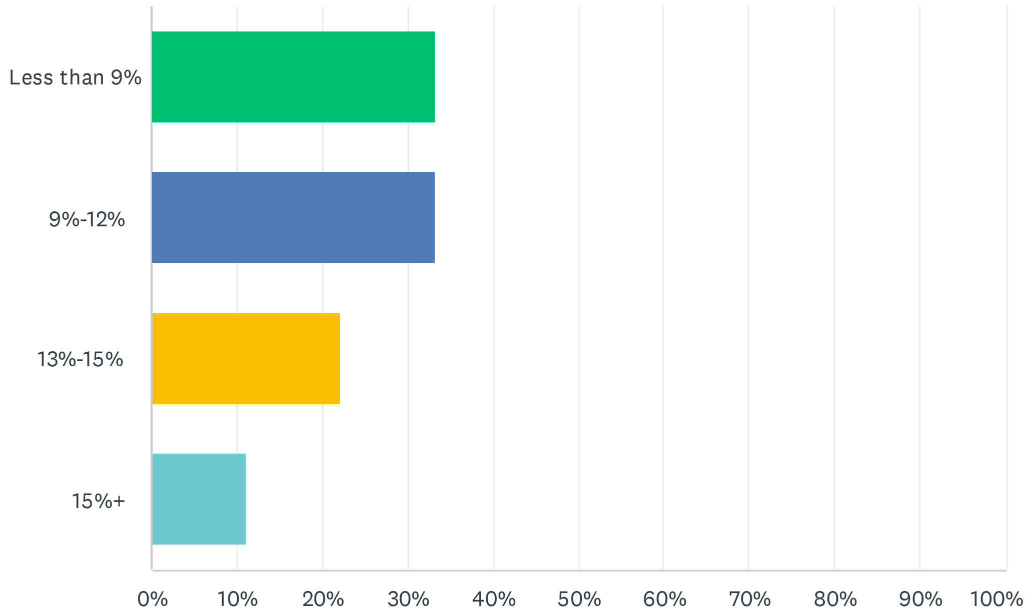
Q7. What net rates of return are you targeting for your private equity and venture capital investments for the 12 months started 1 July 2020?



Answer Choices	Responses	
9%-12%	11.11%	1
13%-15%	0.00%	0
15%+	55.56%	5
Listed equities + 3%	33.33%	3
Listed equities + 5%	0.00%	0
Other (Please outline briefly)	0.00%	0
TOTAL		9

(Answered: 9 Skipped: 0)

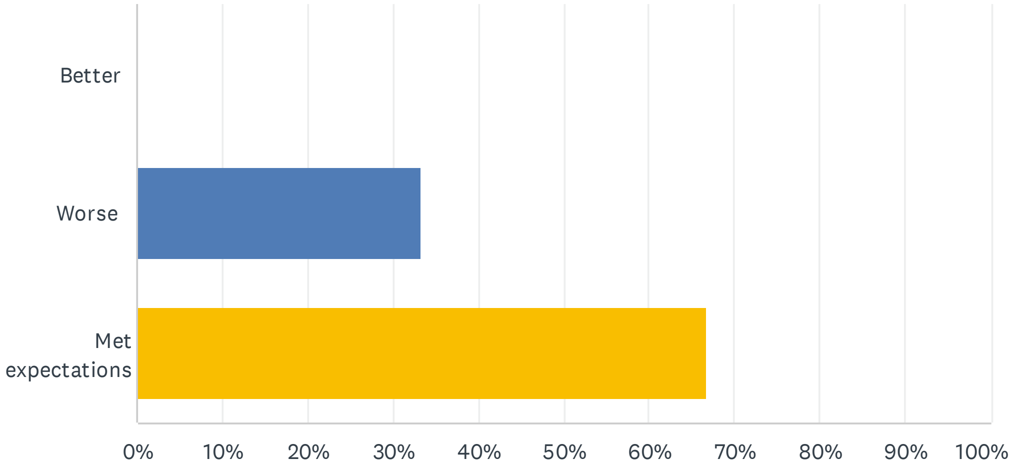
Q8. Historically, what net rates of return have you typically realised from investments in private equity and venture capital?



Answer Choices	Responses	
Less than 9%	33.33%	3
9%-12%	33.33%	3
13%-15%	22.22%	2
15%+	11.11%	1
TOTAL		9

(Answered: 9 Skipped: 0)

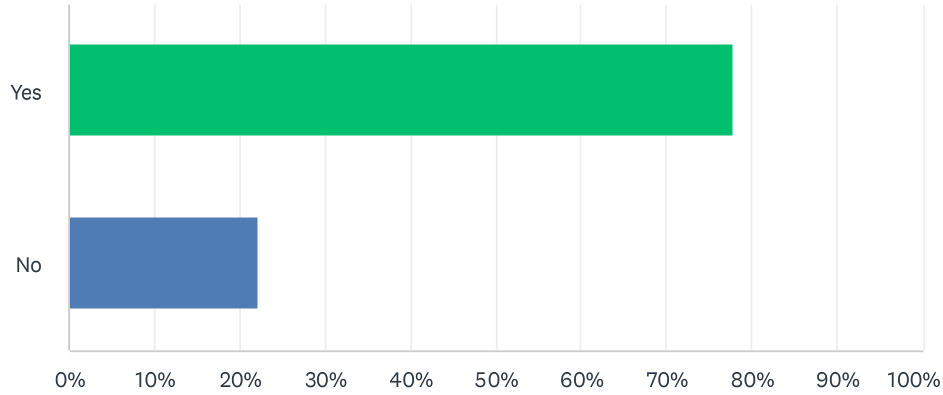
Q9. How have your private equity and venture capital investments performed relative to your expectations for this asset class?



Answer Choices	Responses	
Better	0.00%	0
Worse	33.33%	3
Met expectations	66.67%	6
TOTAL		9

(Answered: 9 Skipped: 0)

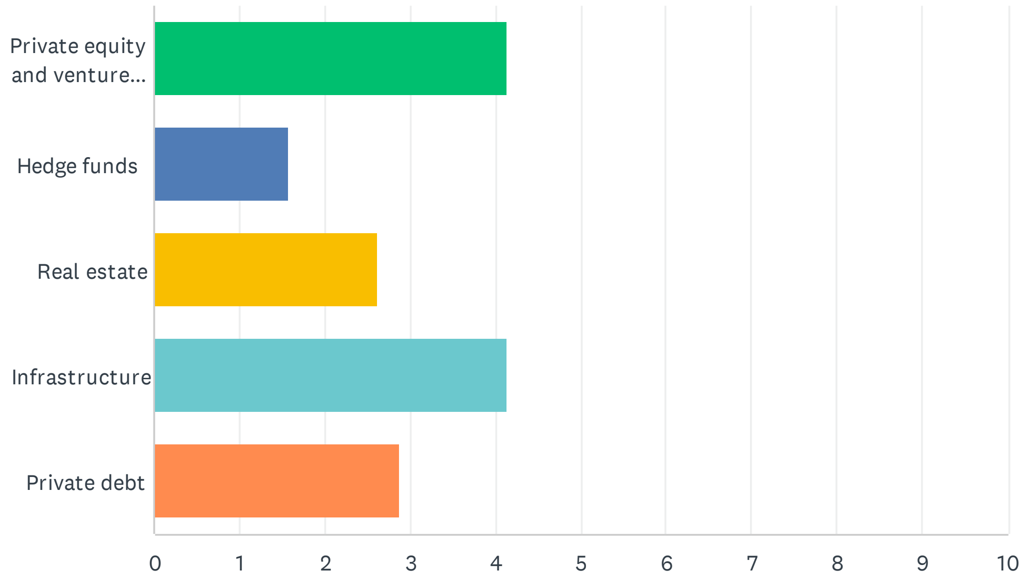
Q10. On a risk adjusted basis, do your current private equity and venture capital investments offer value for money?



Answer Choices	Responses	
Yes	77.78%	7
No	22.22%	2
TOTAL		9

(Answered: 9 Skipped: 0)

Q11. Of the alternative asset classes listed below, rank in order your preferences to allocate funds over the twelve months started 1 July 2020 (1 being of greatest interest and 5 being of least interest):



	1	2	3	4	5	Total	Score
Private equity and venture capital	62.5% 5	12.50% 1	12.50% 1	0.00% 0	12.50% 1	8	4.13
Hedge funds	0.00% 0	0.00% 0	14.29% 1	28.57% 2	57.14% 4	7	1.57
Real estate	12.50% 1	0.00% 0	50.00% 4	12.50% 1	25.00% 2	8	2.63
Infrastructure	14.29% 1	85.71% 6	0.00% 0	0.00% 0	0.00% 0	7	4.14
Private debt	12.50% 1	12.50% 1	25.00% 2	50.00% 4	0.00% 0	8	2.88

(Answered: 8 Skipped: 1)

Q12. What is your level of interest in allocating to direct or co-investment private equity or venture capital investments over the 12 months started 1 July 2020?
(0 indicating no interest and 10 indicating strong interest.)

What is your level of interest in allocating to direct or co-investment private equity or venture capital investments over the 12 months started 1 July 2020? (0 indicating no interest and 10 indicating strong interest
10
5
10
7
0
10
8
10
7
Average: 7.4

(Answered: 9 Skipped: 0)

Q13. What is your level of interest in allocating to Australian private equity and venture capital GPs over the 12 months started 1 July 2020? (0 indicating no interest and 10 indicating strong interest.)

What is your level of interest in allocating to Australian private equity and venture capital GPs over the 12 months started 1 July 2020? (0 indicating no interest and 10 indicating strong interest)
7
5
10
8
0
5
7
10
10
Average: 6.8

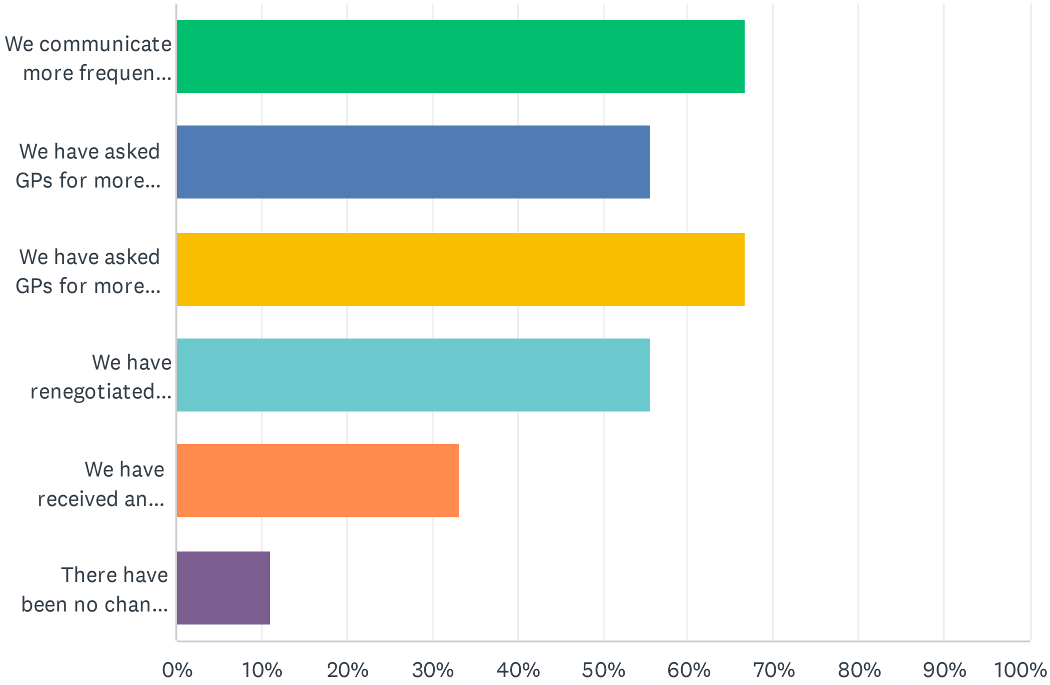
(Answered: 9 Skipped: 0)

Q14. What is your level of interest in allocating specifically to Australian venture capital (as opposed to private equity) GPs over the 12 months started 1 July 2020? (0 indicating no interest and 10 indicating strong interest.)

What is your level of interest in allocating specifically to Australian venture capital (as opposed to private equity) GPs over the 12 months started 1 July 2020? (0 indicating no interest and 10 indicating strong interest)
5
5
5
5
0
3.75
5
10
10
Average: 5.4

(Answered: 9 Skipped: 0)

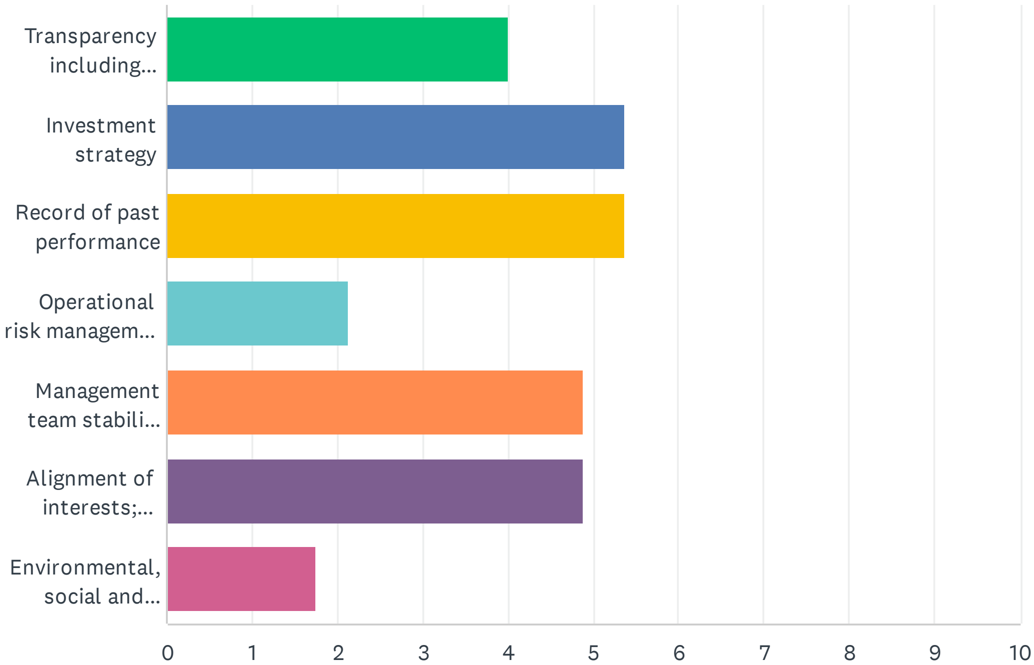
Q15. Reflecting on your relationships with GPs over the last 12 months, which of the following are true? (Select one or more than one.)



Answer Choices	Responses	
We communicate more frequently than previously	66.67%	6
We have asked GPs for more transparency in new investments	55.56%	5
We have asked GPs for more transparency in valuations	66.67%	6
We have renegotiated fees with our existing GPs for their new funds	55.56%	5
We have received an increase in GP extension requests regarding investment periods for the life of funds	33.33%	3
There have been no changes in our relationships with GPs	11.11%	1
TOTAL		11

(Answered: 9 Skipped: 0)

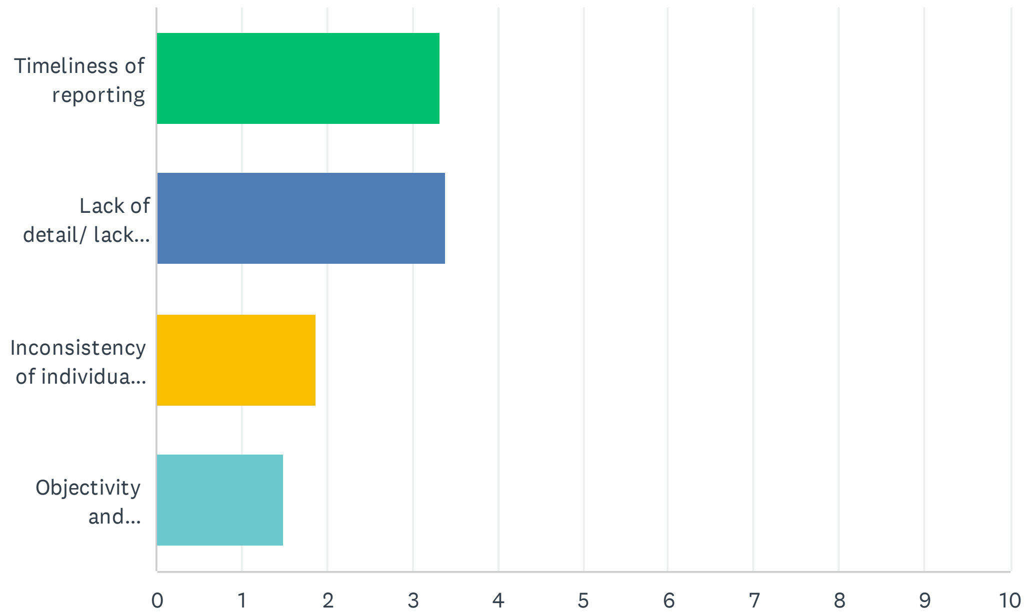
Q16. When allocating to a GP the most important factors are: (Rank in importance with 1 indicating greatest importance.)



	1	2	3	4	5	6	7	Total	Score
Transparency including robust valuation process	11.11% 1	11.11% 1	11.11% 1	11.11% 1	44.44% 4	11.11% 1	0.00% 0	9	4.00
Investment strategy	37.50% 3	12.50% 1	25.00% 2	12.50% 1	0.00% 0	12.50% 1	0.00% 0	8	5.38
Record of past performance	37.50% 3	12.50% 1	25.00% 2	12.50% 1	0.00% 0	12.50% 1	0.00% 0	8	5.38
Operational risk management	0.00% 0	0.00% 0	0.00% 0	12.50% 1	25.00% 2	25.00% 2	37.50% 3	8	2.13
Management team stability and retention strategies	12.50% 1	37.50% 3	12.50% 1	12.50% 1	12.50% 1	12.50% 1	0.00% 0	8	4.88
Alignment of interests; fees, carried interest and GP investment	12.50% 1	25.00% 2	25.00% 2	25.00% 2	0.00% 0	12.50% 1	0.00% 0	8	4.88
Environmental, social and governance (ESG) issues	0.00% 0	0.00% 0	0.00% 0	12.50% 1	12.50% 1	12.50% 1	62.50% 5	8	1.75

(Answered: 9 Skipped: 0)

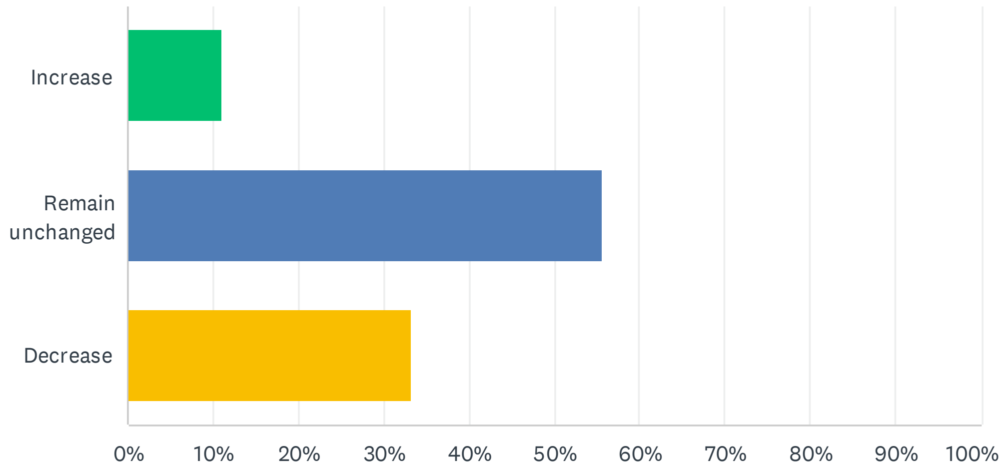
Q17. Regarding valuation and reporting, the most common problems with information received are: (Rank in importance with 1 indicating greatest concern.)



	1	2	3	4	Total	Score
Timeliness of reporting	55.56% 5	33.33% 3	0.00% 0	11.11% 1	9	3.33
Lack of detail/ lack of transparency	50.00% 4	37.50% 3	12.50% 1	0.00% 0	8	3.38
Inconsistency of individual GPs in their reporting from period to period	0.00% 0	0.00% 0	87.50% 7	12.50% 1	8	1.88
Objectivity and independence of those who prepare reports	0.00% 0	25.00% 2	0.00% 0	75.00% 6	8	1.50

(Answered: 9 Skipped: 0)

Q18. How will the new Strategic Asset Allocation (SAA) impact your allocation to private equity and venture capital?



Answer Choices	Responses	
Increase	11.11%	1
Remain unchanged	55.56%	5
Decrease	33.33%	3
TOTAL		9

(Answered: 9 Skipped: 0)

Observations:

Views of the sector increasingly divergent

The average allocation to private equity and venture capital planned for 2020-21 was 5.6%, up from 4.14% in 2019-20 and marginally above the 2018-19 figure of 5.55%.

Changes in the sample from year to year may have influenced those variations, however, it is clear the average has remained below 6% over recent years. The range of allocations in 2020-21 – 2% to 14% – was, however, wider than in 2019-20 so views on allocating to private equity and venture capital are becoming more divergent.

Most to keep allocations unchanged

The largest percentage of respondents (more than 55%) planned to keep allocations to the sector unchanged, or were undecided, whereas in the 2019-2020 survey the largest percentage (50%) planned to increase allocations. The prior survey was completed before the COVID 19 pandemic, so responses were made in a more positive economic environment.

Comments from respondents, however, suggest concerns over legislative changes to the superannuation investment environment such as Your Future Super benchmarking were the primary reason for allocations being kept as unchanged rather than increased. Those planning to increase or decrease allocations were evenly split at more than 20% for each choice.

Funding may flow to new managers

Despite most respondents planning to keep their overall allocations unchanged, more than 55% said they anticipated making fresh commitments so, clearly, they are considering funding new managers. Significantly, only 20% said they did not anticipate making fresh commitments.

Local market gains ground

While most respondents continued to rank the North American market as their first preference for investing in private equity and venture capital in a global strategy, the Australia and New Zealand market was an even closer second choice compared with the previous survey, well ahead of third-placed, and a few years ago second-placed, Europe. Europe, Greater China South-East Asia and South America all lost ground.

High rates of return targeted

The net rates of return targeted for 2020-21 remained high with more than 55% of respondents targeting more than 15 per cent net of fees and more than 30% targeting listed equities plus 3%. In the current low interest rate environment, these expectations may appear possible but, assuming rates will rise a little in the next few years, these expectations may prove to be unsustainable. Current expectations might, therefore, need to be adjusted.

Only 10% targeted less than 12%. This was despite only around a third of respondents saying that historically their returns from private equity and venture capital had been above 13%.

Value for money discounted but still high

Close to 80% of respondents considered that, on a risk adjusted basis, their private equity and venture capital investments offered value for money. This was, however, down from 90% in the previous survey. And, overall, they ranked private equity and venture capital equal first with infrastructure as their preferred alternative asset class. In the previous survey, there had been a marginal preference for infrastructure.

Interest in venture capital slips a little

Interest in allocating specifically to Australian venture capital remained high although slipping from the high of the previous survey. A total of 22% of respondents expressed the highest level of interest, more than 55% reported median interest and 23% negative interest. In the previous survey, 50% of respondents had indicated the highest level of interest, the strongest response in the history of the survey.

Interest in private equity strong but down

Interest in allocating to Australian private equity and venture capital remained strong with 22% of respondents highly interested, 55% expressing median interest and 22% negative interest. This was, however, significantly down on the previous survey in which 25% of respondents had expressed high interest and 60% positive interest.

Specialised investment staff numbers down

Several leading institutional investors took a larger slice of their alternative assets investing in-house over the survey period but the number of equivalent full-time professionals in respondents' private equity and venture capital teams averaged just 2.2. This was down from 3.35 in the previous survey. While changes to the survey sample may have been responsible for some of that change, it is clear that the average size of institutional investors' dedicated private equity and venture capital teams is not increasing and may be shrinking. This is surprising. Capital inflows to the superannuation system continue to grow and mergers among industry funds have substantially increased leading funds' assets under management. Meanwhile the trend towards in-house management of alternative assets investing continues. There appears to be a risk that teams will be under-resourced to deal with direct private equity and venture capital portfolio management.

Commentary

More than 55% of survey respondents reported they planned to keep their allocations to private equity and venture capital unchanged – a significant change compared with the previous survey when 50% had planned to increase their allocations. The previous survey was completed before the pandemic so economic uncertainty caused by COVID-19 and resulting negative economic forecasts have clearly affected confidence since then. But alterations to the superannuation system plus foreshadowed further alterations also probably changed views on the role of illiquid assets in the portfolios of super funds. Allocations to private equity and venture capital also possibly reached a cyclic high point in comparison to other asset classes in the previous survey.

Whatever the precise reasons, responses in the current survey reflected increased economic uncertainty.
It was therefore surprising that most respondents (55%) reported they were still anticipating making fresh commitments

to private equity and venture capital. This was, however, down from more than 80% in the previous survey so still reflected some increased uncertainty.

Despite investors being less enthusiastic about allocating to the asset class, expectations of returns remained high. More than 50% of respondents said they expected returns above 15% net of fees. In the current low interest rate environment, these expectations may appear possible, but assuming rates will rise a little in the next few years these expectations may prove to be unsustainable.

More than 30% of respondent institutions reported historical realised returns of 13% to 15% or above, while an equal percentage reported historical returns of 9% to 12%. It is difficult to reconcile these actual returns with returns of 15% or above expected by more than half of respondents.

More than 75% of respondents considered that, on a risk-adjusted basis, private equity and venture capital offered good value for money. While this was down from 95% in the previous survey, it remained high. Similarly, more than 65% considered that their expectations for the asset class had previously been met. As actual returns were generally below expressed expectations, these responses may have reflected disappointing returns from other asset classes.

As in the prior year, private equity and venture capital was bracketed with infrastructure as the preferred private investment asset class. Private debt and private real estate followed in that order, reversing the order of the prior survey. This reflected interest in investing in private debt growing steadily over recent years.

Interest in allocating to direct or co-investment investment opportunities also followed the trend of recent years and continued to grow.

Interest in allocating to Australian private equity and venture capital GPs remained strong but, surprisingly, after reaching its highest level ever in the previous survey, interest in allocating specifically to Australian venture capital fell.
While more than 60% of respondents were positive about allocating to Australian private equity and venture capital in general, only about 25% were positive about Australian venture capital, although those institutions were highly positive.

Probably even more significantly, about 40% were neither positive nor negative on venture capital, compared with half of respondents expressing positive interest in the previous survey.

This seems counter intuitive in the light of the maturing Australian venture capital sector posting some strong returns over the course of the survey. Perhaps the explanation is twofold: some institutions have made allocations in the past few years and are now allowing time to assess these decisions; and/or in these uncertain times institutions simply consider it prudent to delay entering a new asset class.

Given the challenges of the last 18 months, it was no surprise to learn that LPs were communicating more frequently with GPs and requiring greater transparency into investment strategies and valuations.

Similarly, the continuing focus of LPs on seeking lower fees on new funds, or structuring their private equity exposure to minimise fees, was no surprise in light of the determination of the federal government to keep superannuation funds focused on lowering fees charged to members rather than improving investment returns. This is also a factor in some LPs working to bring all, or at least a large proportion, of their private capital investing in house. As superannuation funds grow ever larger, this clearly becomes more practical but, again, this growth has been accelerated by government pressure on smaller and poorer performing funds to merge with larger funds.

Running counter to this trend, however, is the apparent reluctance of LPs to increase the size of their private equity and venture capital specialist investment teams.

Despite the increase (in dollar value) of capital flowing into the sector, and continued high interest in co-investments, the size of specialist teams remains largely unchanged with most LPs having 1-2 staff, at most, allocated to the asset class. Respondents have increased the weighting of transparency and alignment of interests in their due diligence process, with investment strategy and past performance becoming slightly less important than in the previous survey. Interestingly, the ESG weighting has reduced compared to the previous year.

Timeliness of reporting is considered a bigger problem compared to the previous survey. This may be due to difficulties managers have had during the pandemic in assessing performance of investments as opposed to increasing tardiness by managers.

Interestingly, the new strategic assets allocation (SAA) policy from APRA appears unlikely to change allocations to the private equity and venture capital sector. While, anecdotally, many LPs are suggesting the new policy will have a negative impact on allocations, little change is apparent so far. Perhaps LPs are yet to formally review portfolio allocations in light of the new framework and the impacts are still to come.

About this survey: Private Equity Media sought responses from more than 50 Australian investment institutions known to have invested in private equity or venture capital. Of those, 9 participated in the survey. The survey was sponsored by global financial services provider Apex Group Ltd: www.theapexgroup.com

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