PRIVATE EQUITY

FAST AND FURIOUS?

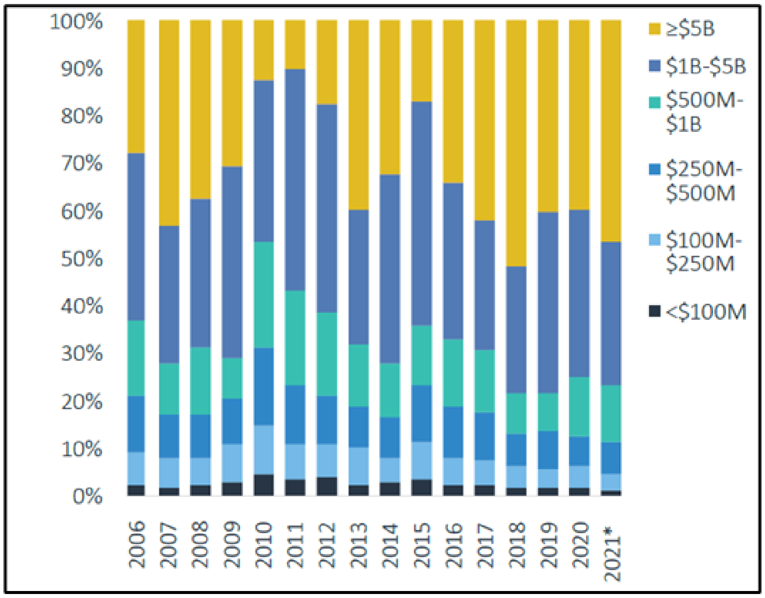
Q4 2021 capped off a record-breaking year of private markets activity and fundraising. According to the Economist, private equity firms signed over 13,000 deals worth over $1.8 trillion heading into the final month of the year. As expected, record levels of cash reserves and a strong financing market drove record activity levels in 2021, and we expect deal activity to continue to be robust in 2022. The technology, media, and telecom (TMT) sector continued to dominate activity, both in terms of value and volume. Total deal value in the sector reached $784.2 billion—nearly double the $404 billion total in 2020, the previous top year on *Mergermarket* record. From health-tech to telecoms, the pandemic added fuel to the fire of existing trends and revealed the extent of the potential for investment, especially in digitalization. Private equity firms will continue to seize opportunities as they look to gain first advantage in high-growth areas. It would not be surprising to expect more firms to join forces in order to achieve the scale and financial clout needed to secure increasingly sizable deals.

Increasingly positive economic conditions such as a brightening global economic outlook, seller-favorable valuations, expected increase in volatility in public markets, and low interest rates are injecting flows into the market. While interest rates are expected to rise, they will likely remain low by historical standards.

The asset class continued to see investors commit capital at an accelerating pace. When total commitments for 2021 are tallied, the year is looking likely to shake out with global totals near or above 2019's pre-pandemic annual record. Many LPs are increasing their allocations to the asset class, drawn by continued outperformance figures in a low-rate environment. Record distributions in 2020 – a result not only of portfolio realizations but of dividend recapitalizations – have allowed LPs to redeploy capital into new funds. According to Pitchbook, the fundraising cycle is also accelerating, with the median time between fund closes continuing to drop, falling to 3.3 years in Q3 2021.

Large institutional investors continue to commit to mega-sized funds, as LPs are looking to streamline their portfolios by allocating to fewer GPs and turning to established firms. Ballooning valuations, especially in the tech sector, are also driving GPs to raise larger funds. The median fund size hit its highest mark in a decade and, as depicted in the chart below, around half of the fundraising dollars YTD have been committed to mega-funds, and two thirds were committed to the fifth or later fund in a fund family. Many sophisticated investors are adding more to their funds and co-investments focused on sustainable and climate-oriented areas. The Covid-19 pandemic, which has made standard due diligence on new funds more challenging – including in-person site visits – has resulted in some LPs being less comfortable to commit to emerging managers. However, RockCreek continues to find new talent in early stage, growth, and buyout with an attractive performance history and continually seeks to discover the next generation of talent, despite the challenges posed by the pandemic.

Private Equity Capital Raised by Fund Size



Source: Pitchbook, (Sept 30, 2021)

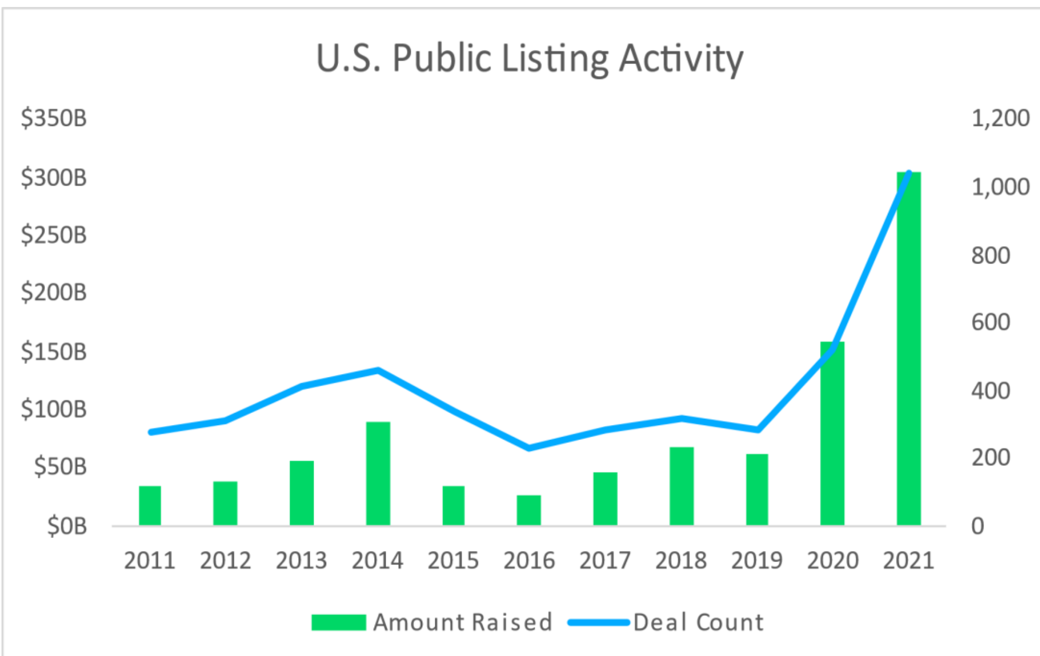
Looking ahead, the pull of the largest private market asset managers doesn't appear to be abating in 2022, with new launches of $17 billion and $27 billion sized funds. While a large number of institutions plow capital into these funds, we have continued to remain focus on GPs that have maintained discipline as it relates to fund size and are seeking to compound their own capital.

MATURATION OF EARLY-STAGE VENTURE.

The venture capital asset class has matured and has increasingly become a staple within an institution's private equity allocation. Venture capital has grown exponentially over the past decade, and it shows no signs of slowing in 2022. According to Pitchbook, in 2021 alone, venture mega-deal activity reached a total deal count of 784 and generated a cumulative deal value of $182.4 billion — a record high compared to just ten years ago, when total deal count was 46 and total deal value was $10.4 billion. Gone are the days when venture was not much more than a cottage industry reserved for wealthy family offices and sophisticated endowments and foundations. Currently, annual early-stage capital investment is well over $150 billion, and more than $110 billion has been raised by venture funds in the US in the last year alone, indicating a more mature, institutional asset class. Interestingly, while many global sovereign funds have increased their early-stage investments, some US pension funds have not been investing in early stage as much.

The maturation of the asset class has, to some extent, accelerated on the heels of shorter holding periods and increased exit velocity. The record-shattering IPO environment of 2021 has greatly increased public market exposure for many VC firms. According to Pitchbook, as of November 29, 2021, 158 VC-backed companies had completed an IPO for a total of $526.1 billion in exit value. The chart below depicts the growth in US public listing activity from 2011 to 2021. In 2021, private companies took advantage of elevated valuations and investor demand to go public, further supported by the SPAC boom, which made the process even easier.

However, LPs have to be cautious, as investing in venture successfully over cycles requires two key ingredients: the ability to discover the next generation of successful venture capital firms and access to the current generation of top-tier venture firms. While the rising tide has lifted all boats – making these factors less discernible – as we enter a new market regime, discovery and access will be critical to continued outperformance. We believe that the market will generate strong returns, and our deep-rooted relationships in the sector and access to some of the best and brightest new talent of our time will matter even more.



Source: PitchBook

The looming question now is how long the IPO window will remain open. Despite the frenetic IPO activity that drove 2021 venture returns and realizations, there is still a strong pipeline of potential unicorns looking to tap public markets and give liquidity to early investors, with the highly anticipated Reddit IPO headlining the potential 2022 class. Some industry observers believe that 2022 could see even more IPOs than last year, although some likely candidates have already begun to consider delaying, given the sudden shift in market sentiment. For example, Justworks, a venture-backed software startup focused on the HR market for small and medium-sized businesses, which had been readying its IPO, announced that it would delay it indefinitely.

IS INDIA THE NEXT CHINA?

Looking outside the US, one area we will continue to focus on in 2022 is growth capital opportunities in India. We believe the market continues to grow and mature, and the current trajectory is not too dissimilar to that seen in China over the last decade. In 2021, the number of Indian unicorns grew by nearly 125 percent. According to AVCJ, investors pumped in $28.2 billion worth of tech investments last year across 779 deals.

As we have mentioned in prior letters, edtech, fintech, and e-commerce were sectors that saw significant investments, and we expect the start-up ecosystem to remain strong in 2022 with the addition of several new unicorns. Several large PE investors have already announced plans to deploy substantial capital in India. Sectors such as insurance (buoyed by recent policy changes allowing foreign investments), construction, real estate, tech, SaaS, fintech, and healthtech will attract substantial investments. Tech M&A will remain strong due to the continued push to digitize, as India remains in its infancy stage, despite having nearly 2.5x the number of internet users as the US.