HOW HAS PRIVATE EQUITY PERFORMANCE COMPARED TO PUBLIC MARKET STOCKS DURING COVID?

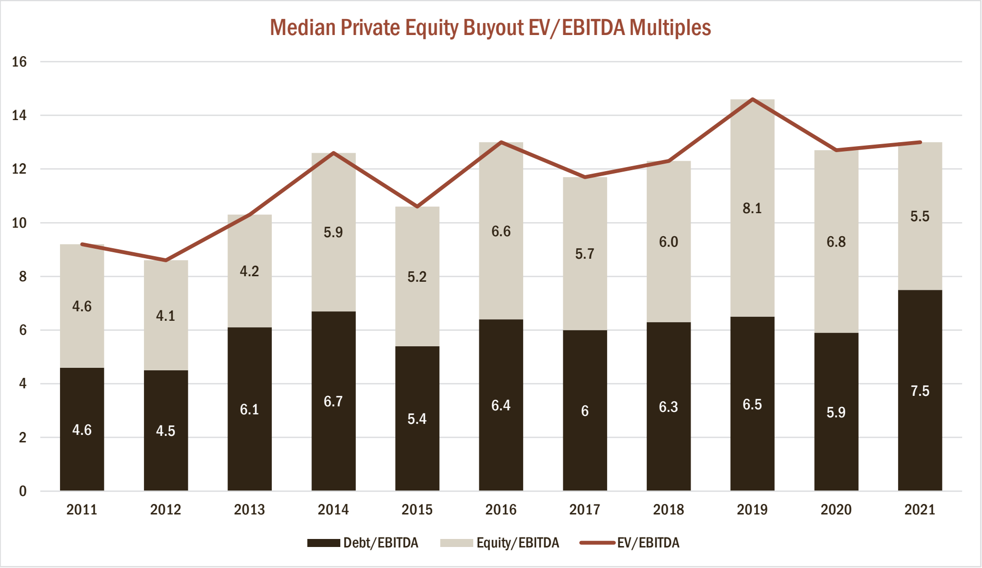
By Adam Emig, CFA®, CAIA, Research Analyst

As COVID-19 began to spread in March of 2020, there were concerns about how the pandemic would disturb not only the publicly traded equities (companies such as Apple that trade on a public exchange and are available to the general public), but also the private investment positions (stocks of companies generally funded by institutions and not available on a public exchange).

Although private investments were markedly down along with the public markets in the first quarter of 2020, they began to bounce back in the second half of last year. The rebound was in part aided by the federal government (CARES Act) and the Federal Reserve's easy monetary policies. We are now witnessing record fundraising and valuations in general across the market.

Private markets fundraising has been strong across all asset classes and is on pace to top the record seen in 2019[1]. This may be attributed to investors' continued appetite for additional yield compared to the relatively lower yields available in public equities, or the opportunity to invest in "unicorn" start-up companies that may one day be the next multi-billion dollar valuation investment.

Deal-making in venture capital, which typically finances startup firms or small businesses believed to have long-term growth potential, and buyouts, usually applied to more mature firms that are acquired by a private equity firm, started to recover in the second half of 2020. Venture Capital remains strong, as cheap debt and ample dry powder in the form of capital awaiting investment both fuel private market funds to consummate deals, in turn elevating valuations. Both early-stage and late-stage venture firm valuations have reached record highs.

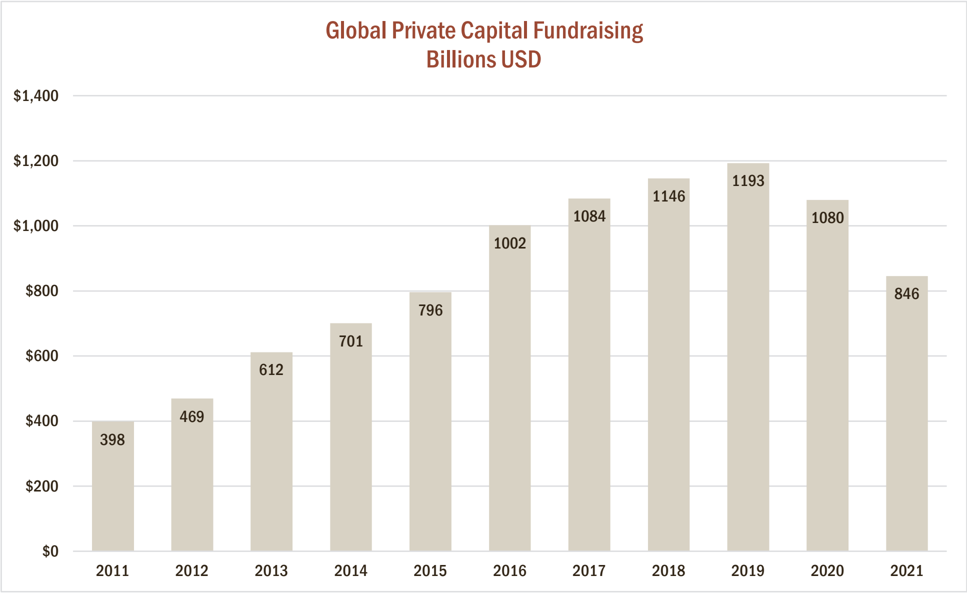


Source Pitchbook
As of June 2021

Participation of crossover funds, which generally are hedge funds that usually invest only in the public markets, along with strong demand from corporations seeking to drive inorganic (investment) growth, helped boost the prices of venture capital fund investments. The IPO (initial public offering) market, in which private companies go public and begin trading on an exchange, also has been robust, producing almost 90% of the exit volumes for venture capital firms.[2]

In the buyout sector, deal-making has been strong across the board, particularly in cybersecurity and health care, both of which have been popular themes in today's environment, which is seeing high demand for new health care options and products and the desire to protect against cyberattacks.

Additionally, deals have been spurred by buyout funds taking advantage of market conditions, including easy credit. This has pushed preliminary 2021 valuations to near-record highs, with EV (enterprise value) to EBITDA (earnings before interest, taxes, depreciation, and amortization) multiples above 12x, and with leverage, the amount of debt the firm owes compared with EBITDA, increasing to 7.5x.



Source: Prequin, J.P. Morgan Asset Management

*Includes private equity, private debt, infrastructure, real estate and natural resources

Performance in the private markets has been strong and has seen similar returns to public equity markets as economies re-opened in 2020 into 2021.

The latest data (as of December 2020) from PitchBook, a leading provider of private market data, showed buyout/growth equity funds produced a 13.8% one-year return, while venture capital was up 20%. These figures compare with the S&P 500 Index return of 18.4%. The private markets lagged public markets during the early rebound in 2020. It appears that initial trend has turned, with private markets starting to outperform their public peers. Preliminary first quarter 2021 returns were 11.5% in buyout/growth equity funds and 16.2% in venture capital funds versus the S&P 500 return of 6.2%.[3]

As a result of strong demand for private investments and favorable market conditions, valuations and debt levels have been pushed to near-record highs, similar to what we have seen in public markets. This is a development worth watching, as private investments are a growing part of the investing universe.

It is always important to remember to consult with an investment advisor, especially when a new investment vehicle may have some complex aspects, so that your portfolio reflects your long-term investment goals over time. Always feel free to reach out to your Commerce Trust portfolio manager to discuss these matters to achieve a long-term outcome consistent with your objectives.

[1] J.P. Morgan, "Guide to Alternatives," 3Q 2021, p. 3.
[2] J.P. Morgan, "Guide to Alternatives," 3Q 2021, p. 5.
[3] Pitchbook Data, Inc., "U.S. PE Breakdown," Q2 2021, p. 5.

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Adam is a senior investment research analyst for Commerce Trust Company, responsible for manager due diligence covering liquid alternatives and taxable fixed income managers and co-leading the Commerce private investment program. Adam joined Commerce Trust in 2020. He previously worked for five years at Mercy Investment Services, the asset management firm for the Sisters of Mercy of the Americas, where he served as senior investment analyst, helping manage the organization's private market, hedge fund, equity and fixed income investments. Additionally, Adam spent seven years at Scottrade, Inc., in various capacities. Adam holds both the Chartered Financial Analyst® and Chartered Alternative Investment Analyst designations. Adam volunteers at and serves as president of the Robert L. Emig Foundation, which promotes the well-being of at-need youth through sports and education.