Moonfare Investor Survey 2022
White paper

Patience and *persistence*

Moonfare®

About the survey

In September 2022, we conducted an online survey to better understand the sentiment of Moonfare's investor community. We are grateful to the 244 Moonfare investors who offered us their views and observations about private equity investing in the given economic circumstances. Respondents were individual private equity investors, domiciled in Europe, US and Asia. All data was collected anonymously and has been aggregated. Note that percentages may not add up to 100 percent, as they are rounded to the nearest percent.

Contents

A glimpse into the future: the investment themes shaping the world

It can be hard to think about the world beyond this year's headlines. The current events, especially the tragic war in Ukraine and the uncertain and volatile economy rightly demand our full attention.

At the same time, we are in a business that requires long-term thinking. Personally and professionally, I'm interested in investment opportunities that transcend economic cycles and current news. For this reason, I believe that private equity is well placed to support and capitalize on some of the great economic themes of the decade. Here, I am highlighting three:

Technological transformation

Technology has shaped the economy for decades and regardless of recent valuation fluctuations it will continue to dominate. McKinsey believes we will experience more technological progress in this decade than we did in the preceding 100 years put together.[1] The market for artificial intelligence alone is projected to reach $4.5 trillion by 2025 and the demand for blockchain solutions could surpass $1.2 trillion by 2030.[2] Digital transformation is particularly imperative in today's economy – as capital costs rise, companies have to invest more into productivity gains to remain competitive. All this translates into enormous investment opportunities in an industry characterized by high margins and quickly scalable products and services.

Supply chains

Global supply chains have come under immense pressure recently, exposing critical vulnerabilities. The upside is that this has generated a spate of innovation to address these challenges, supported by massive amounts of capital. Some of the solutions include autonomous delivery, fulfilment tech and intelligent warehousing. Private equity, in particular, has its eye on storage and distribution businesses – the enablers of e-commerce.[3] The retail side of e-commerce alone is projected to increase by 40 percent in the next four years, inevitably requiring ever-growing logistical capacities.[4] Supply chain systems are going through a fundamental transformation from where they'll emerge more agile and efficient.

Energy transition

Massive resources are earmarked for what is probably going to be the project of our generation and generations to come – a transition toward a low-carbon economy. Achieving net zero on a global scale is expected to cost around $125 trillion in climate investment.[5] In 2021, we already spent $755 billion on deploying low-carbon energy technologies, up 27 percent year on year.[6] It's hard to even imagine how massive this shift is: the transformation of the world's energy model will undoubtedly unlock vast new economic opportunities.

Private investors will play a key role in financing these and other themes, helping to transform the global economy into one that's more resilient, productive and sustainable. Indeed, the market for private equity, venture capital (VC) and other alternatives is expected to explode in the coming years — largely thanks to the growing participation of retail investors.[7] For me, the attractiveness of the asset class is clear: private equity not only offers the potential of outsized risk-adjusted returns but also provides investors with one of the best ways to contribute to a meaningful change in the world.

Dr. Steffen Pauls
Founder and CEO of Moonfare

Key highlights

1 Growing concerns amid *recession woes*

The global economy is in for tougher times. Retail investors in private equity share concerns about the immediate economic outlook, too. They also expect a prolonged slowdown which could extend well into 2023 and beyond.

2 Confidence in *private equity* remains high

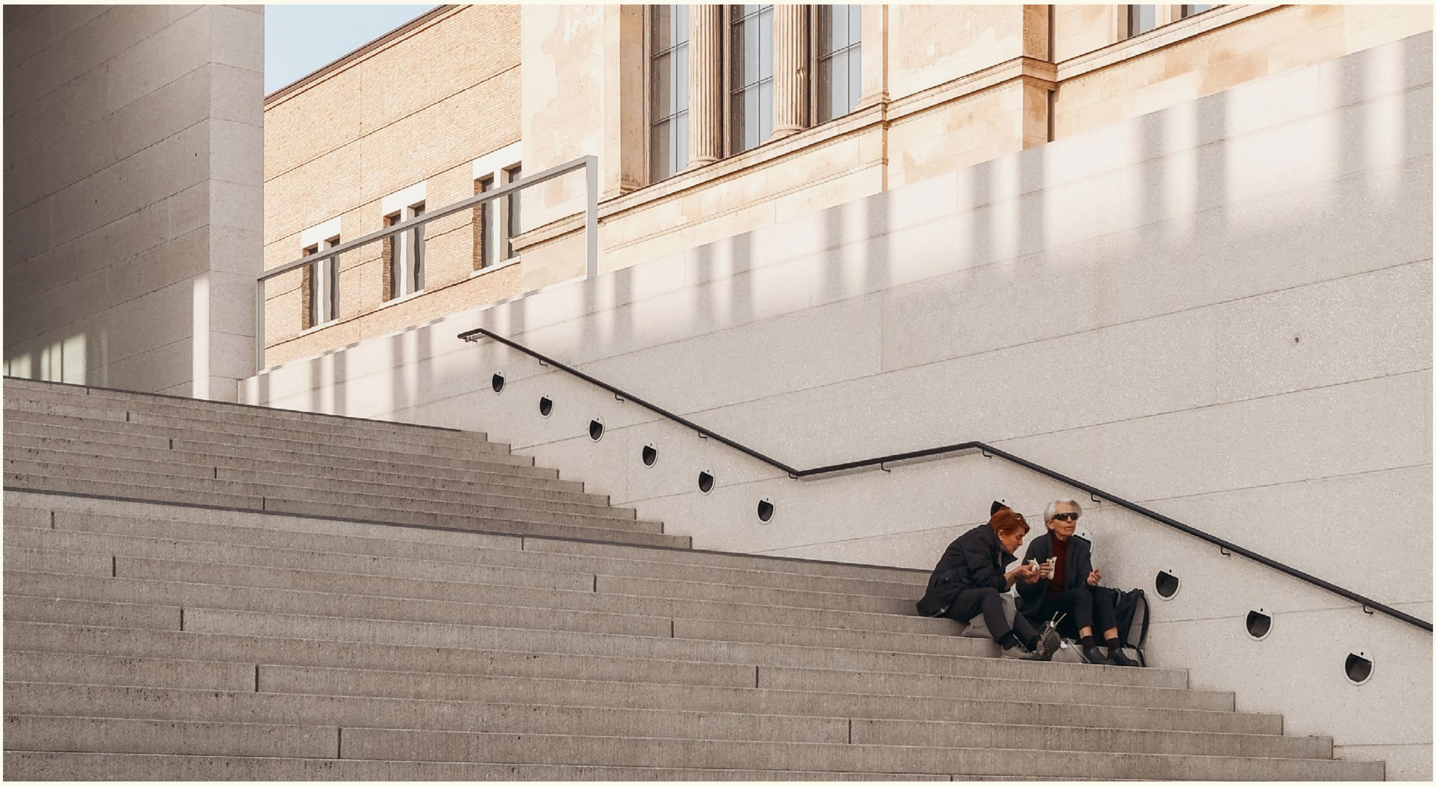
Investors are doubling down on private equity, despite the macro headwinds – 83 percent are considering making new allocations to the asset class in the next 12 months. They're already well exposed to private market assets and are aiming to further increase their share.

3 Spotlight on *buyouts* and *defensive strategies*

Traditional buyout funds are seen as the best bets in today's economy. Infrastructure, secondaries and private credit are also on investors' radars given their recession-resilient traits. Conversely, there's less confidence in tech-heavy VC and growth.

4 Investors love a good track record, but see illiquidity as the *biggest barrier*

When making an investment decision, retail investors will first consider the track record and then the fund's leadership team. Illiquidity, fees and long-term horizon are the biggest hurdles but there are good ways to mitigate their influence.



As *recessionary forces* loom, focus turns to *macro risks*

Investors are bullish on private equity, our survey shows, however they're aware that economic challenges lay in the near future. Indeed, decision-makers around the world are grappling with intense headwinds, leading the global economy into what will likely be a period of volatility and decreased economic activity. It is understandable, therefore, that many investors have dwindling confidence in the economic outlook. Around three-quarters of respondents say they feel "somewhat bad" and an additional 12 percent perceive the economy to be in a "very bad" condition currently (figure 1).

Indeed, there's ample evidence that the global energy and inflation crises may be tipping leading economies into recession.[8] The US economy contracted this year[9] and global growth is projected to remain subdued[10] while stocks are on track for their worst year since 2008.[11] To bring inflation down to the target two percent level, central banks are expected to keep the rates rising through 2023 and possibly beyond.[12, 13] These and other forecasts are echoed across private markets. When asked about how long they predict the slump to last, 62 percent of respondents in the survey answered between one to two years (figure 2).

Investors have also expressed some unease with developments more specific to private markets. A third worry about rising borrowing costs, and almost a quarter feel the same about potentially slower deployment rates. The two concerns are intertwined – higher financing costs and more caution from lenders when providing loans to leveraged buyouts could make transactions harder to close.

Indeed, the supply of syndicated institutional loans and high-yield bonds across the US and Europe — the key sources of debt financing for private equity deals — cratered by 72 percent over the first nine months of 2022.[14] Private equity deal activity is also down and is expected to decrease further as pipelines of high quality deals soften.[15] This decline is exacerbated by an expectations gap between sellers and buyers, which is typical in periods of increased volatility – buyers are pressuring for lower entry multiples and sellers wait for a better time to sell. In addition, price increases are now hardwired into deal decisions. Companies that can't pass on higher costs to the consumer are likely to be shunned by dealmakers, further shrinking the pool of suitable targets.

The bar for investment has clearly gone up. However, fund managers may well be better positioned to manage the increased cost of capital than they were a decade ago. For existing investments, fixed-rate financing will provide some room to revisit capital structure before refinancing. For new investments, meanwhile, interest rate hikes will be priced into entry valuations with likely lower leverage.

62%

of respondents predict the downturn to last between one to two years.

Figure 1: The economy is heading for recession and investors share concerns

↻ How do you feel about the current state of the global economy?

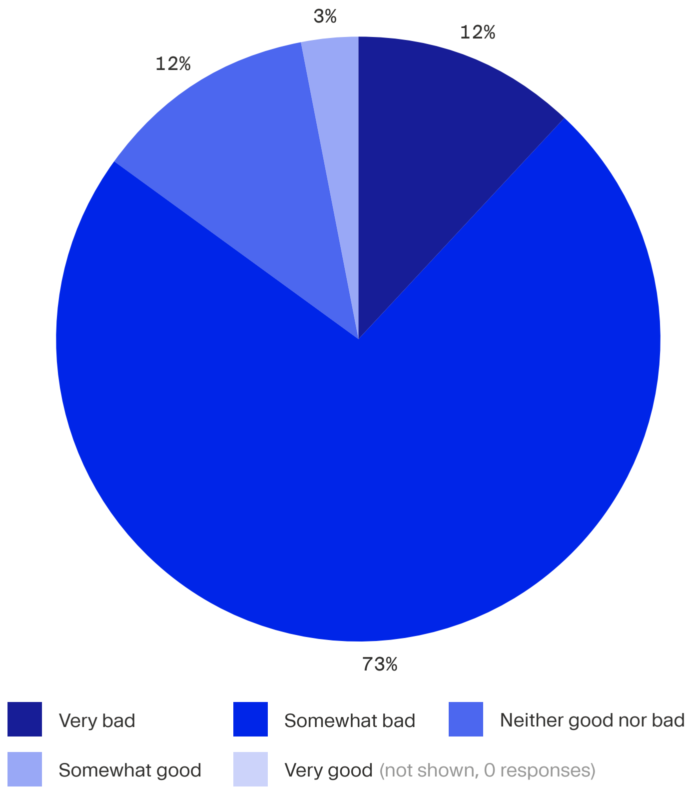


Figure 2: Most investors don't expect the downturn to end next year just yet

↻ How long do you think the economic downturn will last? (as of September 2022)

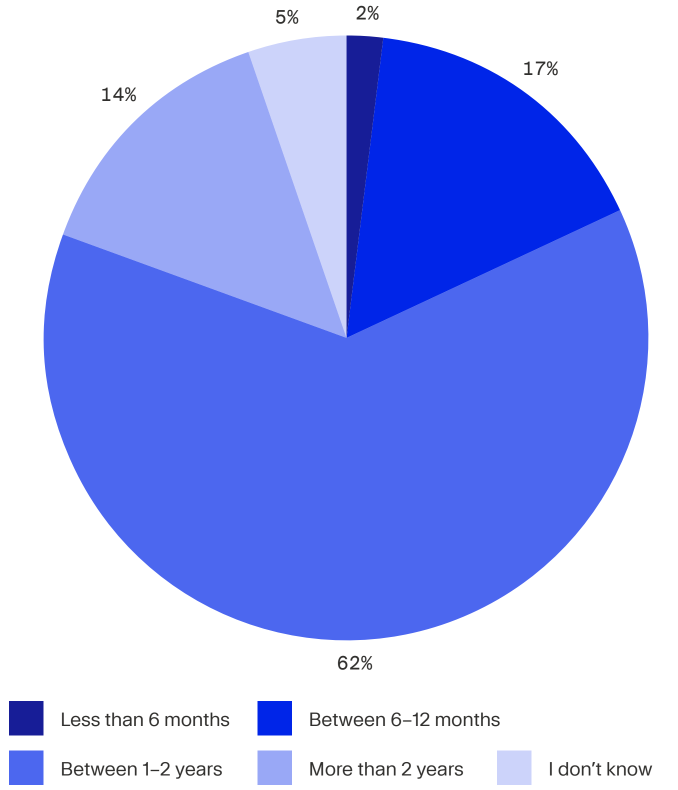
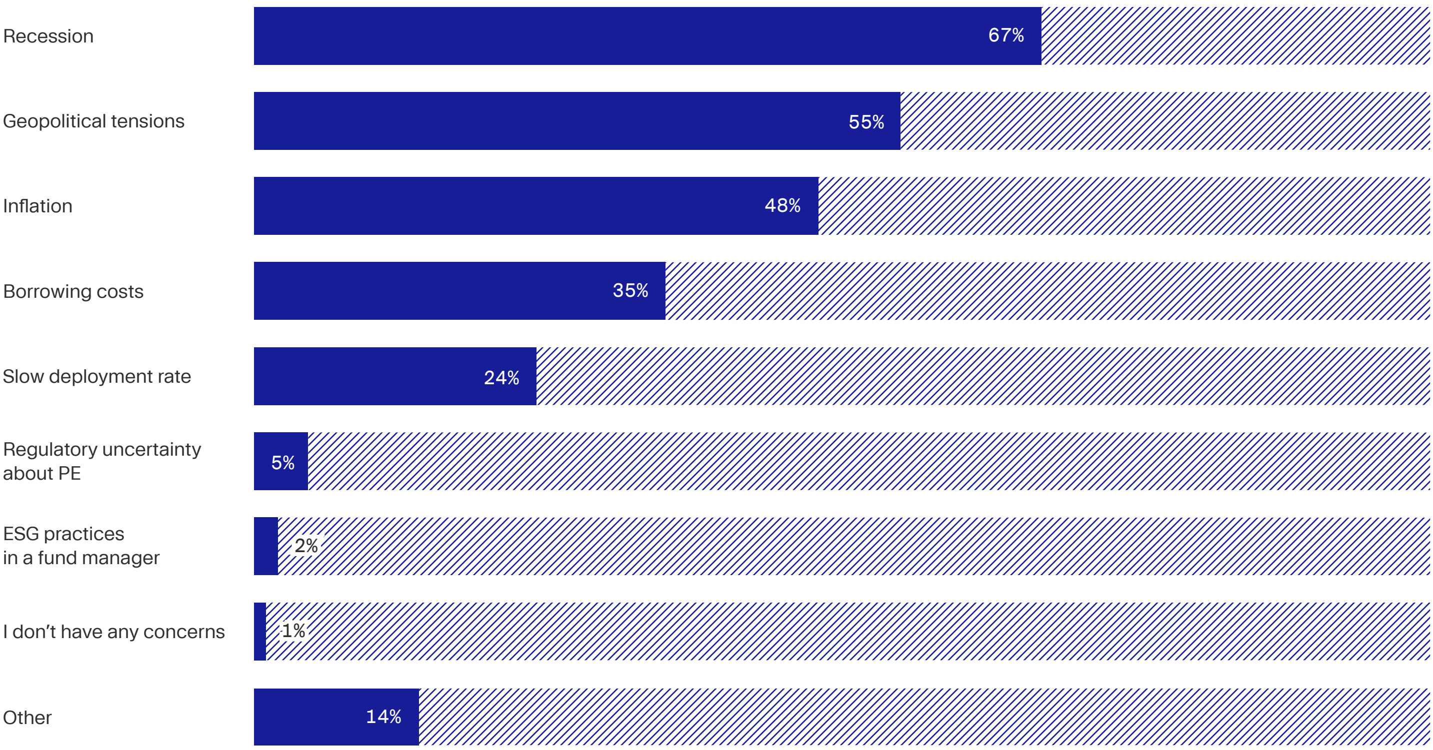


Figure 3: Recession, war and inflation weighing on investors' minds

↻ Considering your private equity investments, what are the biggest concerns you have? Select up to three answers.



Private equity investors are *standing their ground*

Despite the rocky economic outlook, our survey respondents are optimistic about the future of their private equity portfolios. An overwhelming majority (77 percent) predict their investments will meet expectations and eight percent expect their investments to exceed them.

Respondents consider private equity a high-conviction bet given the circumstances. Eighty-three percent intend to increase their investment in private equity over the next 12 months. At the same time, only a small percentage report that they're adopting a wait-and-see stance with eight percent considering holding off on investments and ten percent being undecided (figure 4).

Figure 4: Going long on private equity – despite the downturn

How much do you plan to allocate to private equity in the next 12 months?

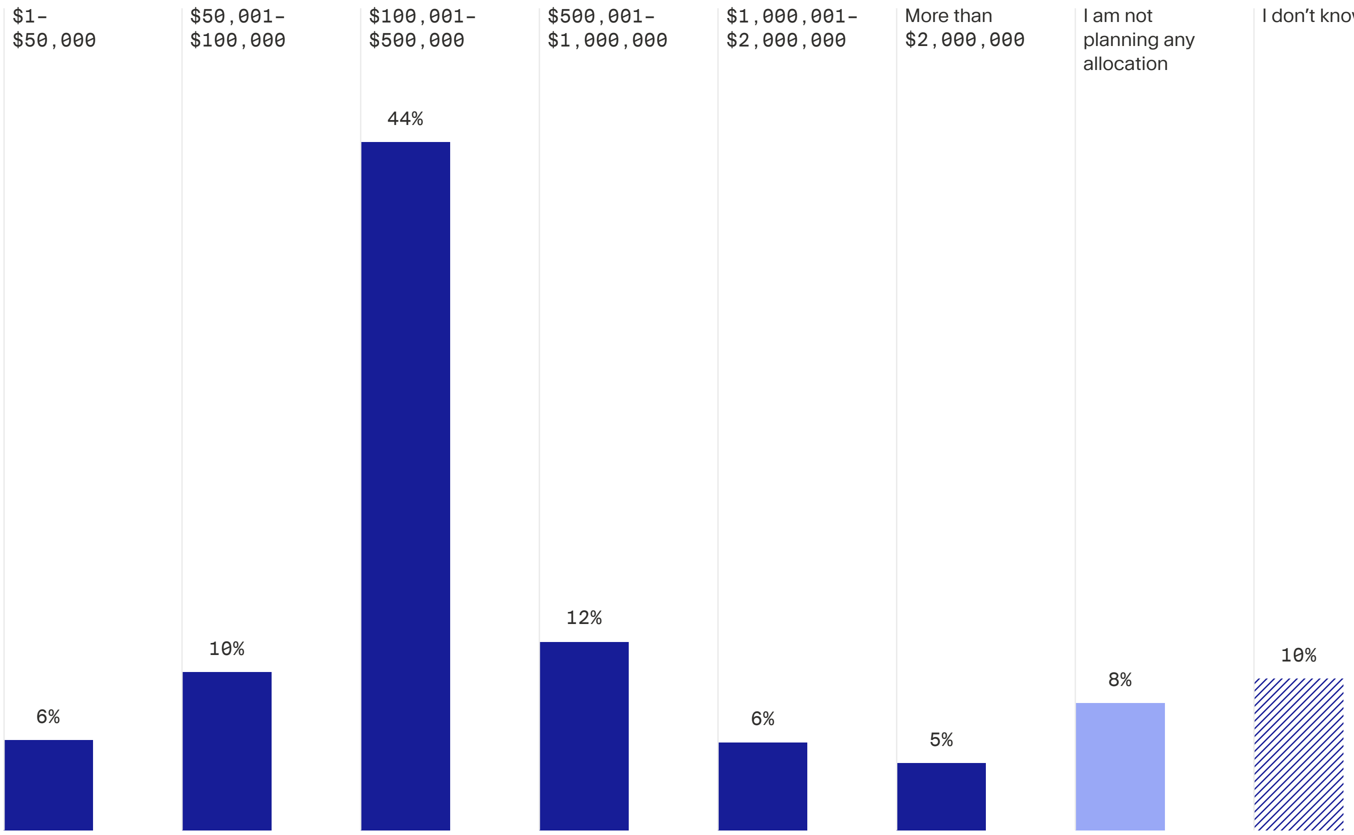
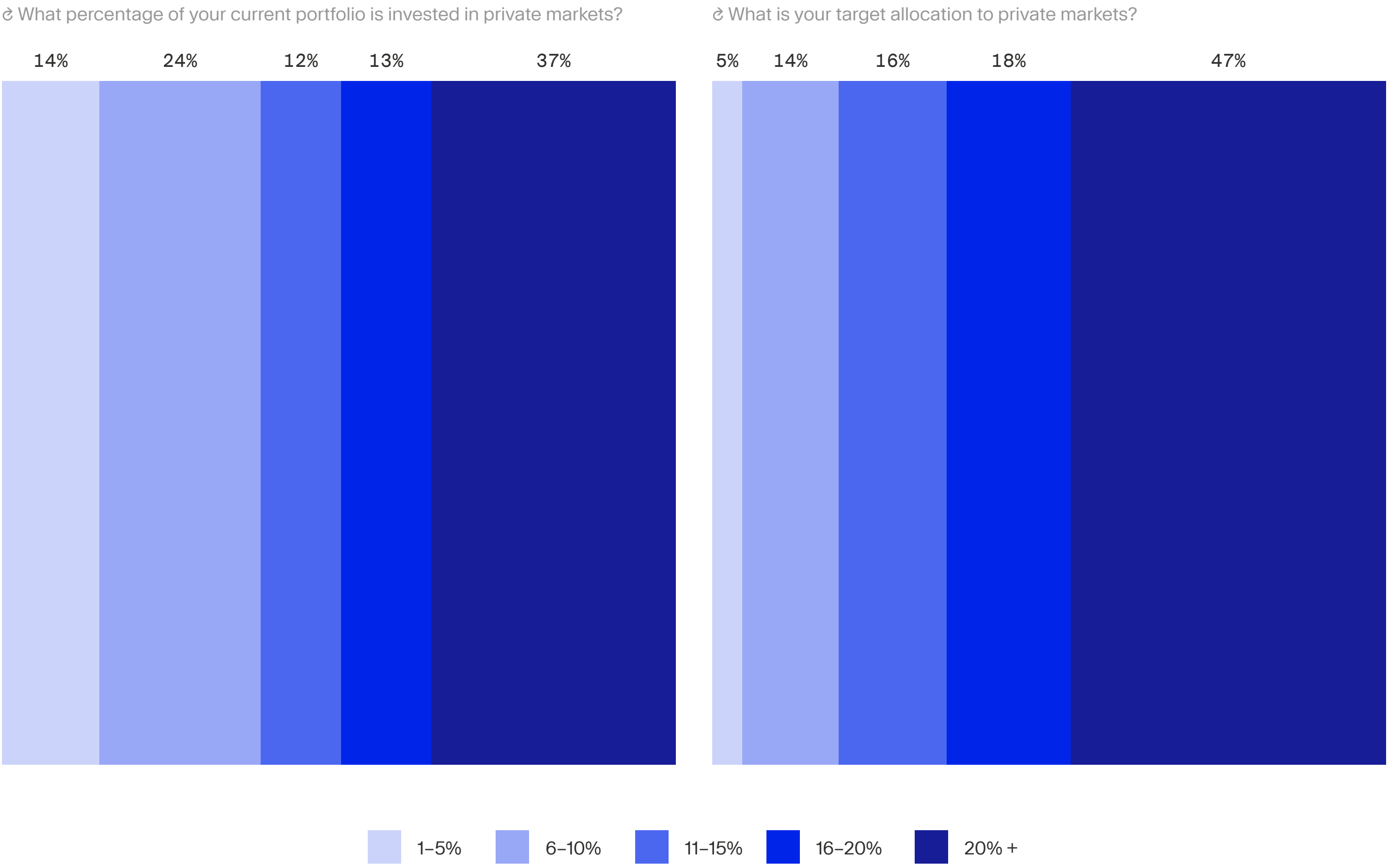


Figure 5: Making space: Big plans for private markets in investors' portfolios



These relatively buoyant expectations for private equity reflect a broader belief that the asset class's inherent characteristics make it well-placed to survive and perhaps thrive when wider markets turn for the worse. Even more, firms that can secure high-quality acquisitions at lower entry multiples may see outsized returns by the time markets rebound and the exit window opens up again.

Survey participants also report relatively high exposure to private markets, while some on the lower end have indicated plans to further increase private asset share in their portfolios. Around 37 percent say that a fifth of their portfolio or more is currently invested in private assets (figure 5). This puts them in the allocation ranges of institutions with more established private market history, such as pension funds and wealth managers.[16]

83%

of respondents intend to keep investing in private equity in the next 12 months.

These figures underscore a trend we've been observing for the past few years. In search of higher returns and diversification benefits, investors are leaving behind traditional methods of portfolio construction in favour of adding private assets. This comes with good reason – between 2000 and 2020, a portfolio with a larger allocation to private equity and private credit offered almost two percentage points higher returns than a traditional portfolio comprising 60 percent equities and 40 percent bonds, according to research by Hamilton Lane.[17]

The shift is only accelerating, reflected by the personal target allocations that survey participants have set. Almost half aim to have a fifth of their portfolios invested in private assets, with an additional 34 percent who have earmarked between 10 percent and 20 percent (figure 5).

Investors need to keep in mind, however, that the size of the excess return largely depends on the fund selection. In a 2021 PitchBook analysis, the top-performing-quartile excess return was 0.9 percent — more than double the lower-quartile excess return of 0.4 percent.[18] During turbulent economic times, the performance gap between top and bottom quartile vehicles is only amplified.[19, 20]

Spotlight on *buyouts* and *defensive strategies*

Across the broader market, investors are shifting focus to favour strategies considered more recession resilient. Forty percent of survey respondents expect infrastructure funds, for example, to generate the best returns in the short term. At the same time, however, the beliefs of investors don't seem to yet match their actions – only 15 percent are currently invested in infrastructure (figure 6).

Infrastructure's attractiveness largely originates from the industry's high entry barriers and the ability to pass raising costs to consumers through concession agreements or contracts, potentially providing investors with a certain hedge against inflationary pressures.[21] Indeed, infra funds have proved popular with investors so far, raising a record $113 billion in the first half.[22]

Secondaries, too, are starting to pique the interest of a broader group of investors. Around 37 percent of respondents believe they are one of the top three private market strategies in current market conditions, roughly levelled VC, growth and infrastructure but way ahead of real estate, credit and impact.

Secondaries give investors a recourse to liquidate assets before the end of the fund lifecycle and can function as a lever for more sophisticated cash-flow management. Incoming investors at the other end of the marketplace tend to invest in secondaries to buy existing private equity commitments, often at discounted prices. Secondaries are also an attractive tool for general partners, allowing them to extend ownership of high-quality assets beyond the typical holding periods. This way, fund managers can maximize the value of investments they consider best in class.

Overall, however, traditional buyout funds are still perceived as solid options in today's economy. Their track record from past downturns substantiates the outlook – deals coming out of past recessions have delivered outsized relative returns. Following the dot-com crisis, for example, buyouts generated a median internal rate of return (IRR) of 40 percent in 2002 and 47 percent in 2003. After the global financial crisis in 2009, they produced a 24 percent IRR.[23] Much of the strength of buyout funds is rooted in their fundamentals: active ownership, employing value-add capabilities and providing flexibility in capital deployment.

While investors have confidence in the robustness of buyouts and certain other strategies perceived as defensive, there is some consternation about more risk-on asset strategies, such as VC and growth equity. Survey respondents are generally well exposed to these tech-heavy strategies, but are less convinced about their near-term performance.

This is understandable, as VC and growth have experienced steep declines in fundraising and valuations this year. Venture funding in Q3 totalled $81 billion, down 53 percent compared to same period last year, and median valuations had declined across most investment stages, most notably in pre-IPO rounds.[24, 25]

77%

of respondents consider tech as one of the most promising industries to invest in.

It's important to note, however, that last year's entry multiples were close to historical highs, and despite current markdowns, tech valuations in Q3 remained 35 percent higher than they were in 2020.[26] Considering this perspective, the reset so far could be seen as a rebalancing act towards a new environment while investors adjust to more moderate growth expectations with a focus on profitability.

This outlook is underscored by the broader appeal of technology. More than 77 percent of survey respondents consider tech as one of the most promising industries to invest in, followed by healthcare (72 percent, figure 7).

Indeed, we are still in the early stages of digitisation, a process which will remain a key growth driver, underpinned by secular trends such as demographic shifts and changes in consumer behaviour.

For example, experts widely consider that artificial intelligence (AI) solutions could fundamentally transform the productivity and GDP potential of the global economy in the years to come.[27, 28] According to estimates, the market for AI is projected to grow ten times and reach $1.4 trillion by 2029.[29] Investing in technology therefore requires a long-term view and acknowledgement that emerging ideas of today will shape the economic landscape in ten years' time.

Figure 6: Buyouts remain the favourite, while recession-resilient strategies move to the forefront

In which private market strategies are you currently invested?

In your opinion, which three private market strategies will perform the best given the current economic conditions?

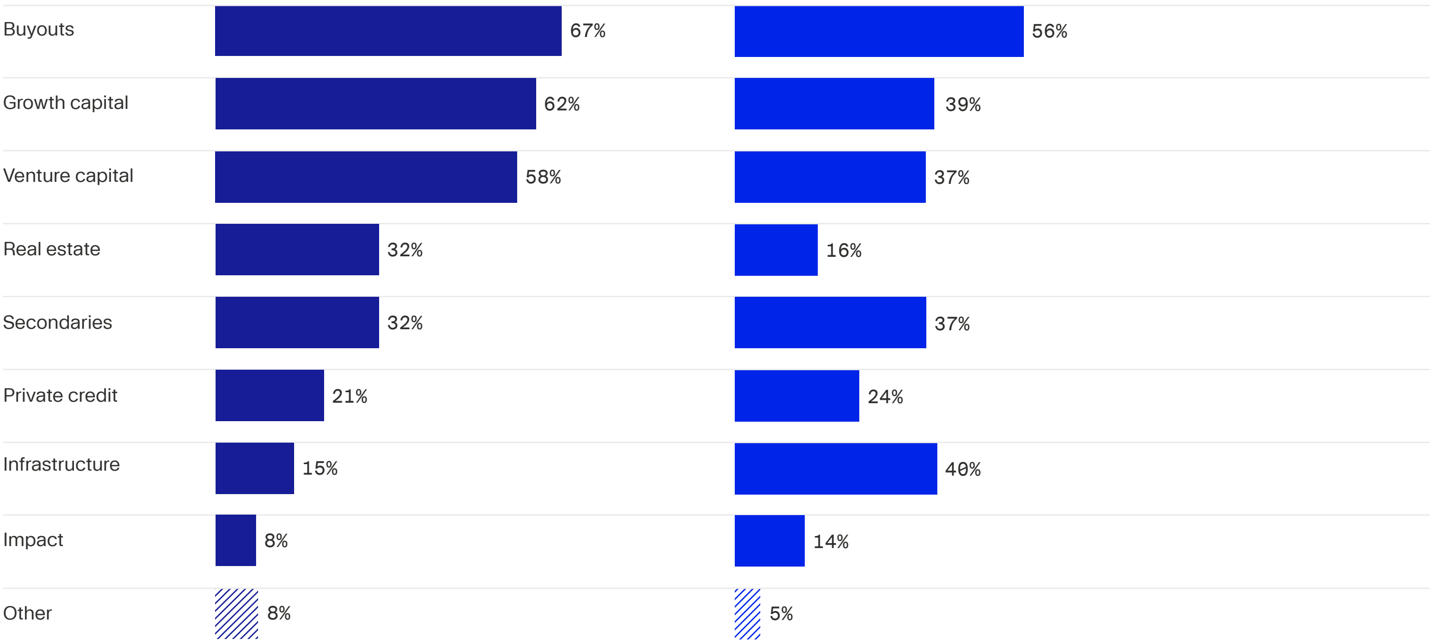
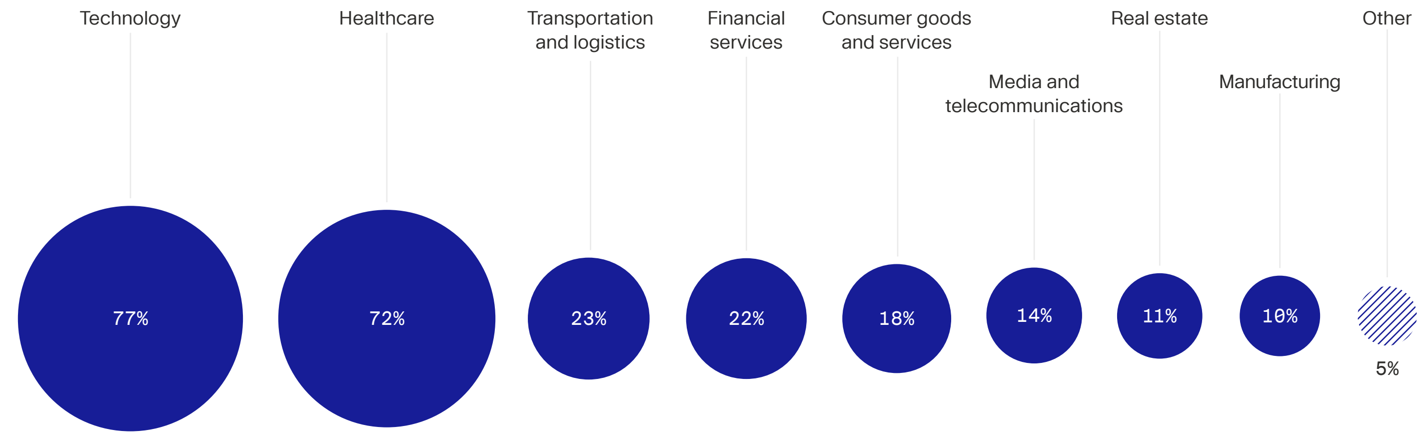


Figure 7: Applying the long-term lens, appetite for tech remains strong as ever

Which of the following industries do you consider most promising to invest in? Select up to three answers.

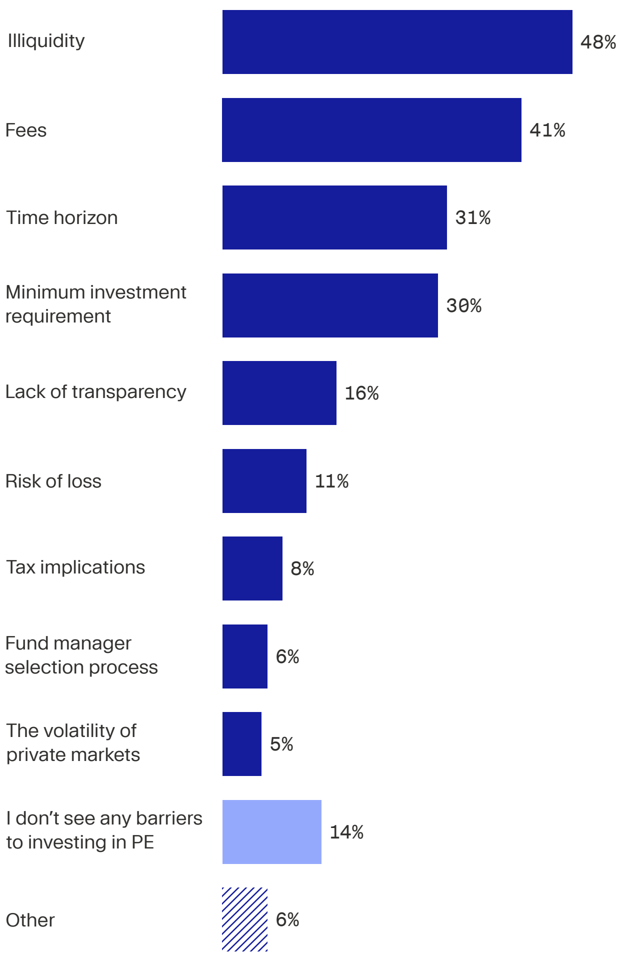


The door to private equity is *open*, but barriers *still exist*

Once only a preserve of institutional allocators and family offices, private equity is rapidly opening up to a broader market of individual investors. That said, barriers to entry still exist – and some are inherent to the asset class.

Figure 8: Illiqudity and fees keeping investors from writing bigger cheques

Which factors prevent you from investment more in private equity? Select up to three answers that apply to you the most.



Private equity hurdles and how to overcome them

When asked about what prevents them from making higher allocations to private equity, almost half of the Moonfare Investor Survey participants ranked illiquidity as one of the biggest hurdles. This was followed by fees (41 percent) and the longer time horizon (31 percent, figure 8).

Indeed, private equity is an illiquid asset class and significant commitments are typically locked in for several years. But being patient with your private equity investments is also key to getting rewarded. On average, investors receive up to five percent premium for illiquidity, according to Barclays estimates.[30]

There are also various ways to mitigate some illiquidity concerns. In a more mature portfolio, investors can reinvest profits from one private equity investment to fund the capital calls from new fund investments, effectively creating a self-funding portfolio. On average, it takes four to five years for a mature portfolio to become self-financing.[31] It's also worth remembering that investors' capital is not called in one lump sum but rather every time the fund identifies an investment opportunity. This offers investors flexibility to invest the capital elsewhere until it's called.

In addition, an investor's cash flow can be optimised by adding secondary investments where distributions are expected earlier compared to primary investments.[32] Investors can buy stakes in more mature portfolios with shorter holding periods and potentially earlier cash returns. To address these liquidity needs, more and more secondary market solutions are emerging. Moonfare, for example, offers its secondary market where investors can sell their interests before the end of the fund's lifecycle.*

* Liquidity via the Moonfare secondary market is not guaranteed.

The minimum investment requirement is another important consideration for private equity investors, according to the Moonfare survey. Although the threshold for gaining private equity exposure is still relatively high compared to public markets, minimum requirements have dropped significantly in the last few years, largely thanks to the emergence of tech-enabled solutions. Moonfare, for example, enables investments in private equity, with minimums of committed capital as low as €50,000. It is expected that private markets will be made accessible to an even broader group of individuals, also on the back of products tailored specifically to the needs of the retail market.

5%

is the illiquidity premium in private equity.

Source: Barclays

Fund red flags

Survey respondents are most likely to steer away from funds that invest in markets or products they don't support (figure 9). This sentiment is consistent with the rise of value-driven propositions such as impact investing, which sees investors aligning their portfolios with environmental, social and governance considerations.

Other red flags investors look out for when it comes to private equity investing include the lack of track record. Investors want to tap into the knowledge and experience of cycle-tested fund managers who have maintained performance and continue to identify investment opportunities even in market downturns.

More recently, the (in)ability of fund managers to deploy raised capital has come to the fore. Despite the current market dislocation, the fund lifecycle can't be put on hold, and with so much dry powder[33] chasing a smaller pool of high-value investments, some firms may find themselves scrambling for deals. This challenge might evolve into a more significant problem for individual managers who have raised significant funds but lack the required sourcing and operational capacities to deploy capital. Replicable and scalable processes are therefore crucial to avoid this type of diseconomy of scale.

Figure 9: Saying 'no' to funds with different investment views

What prevents you from investing in a particular private equity fund? Select up to three answers that apply to you the most.

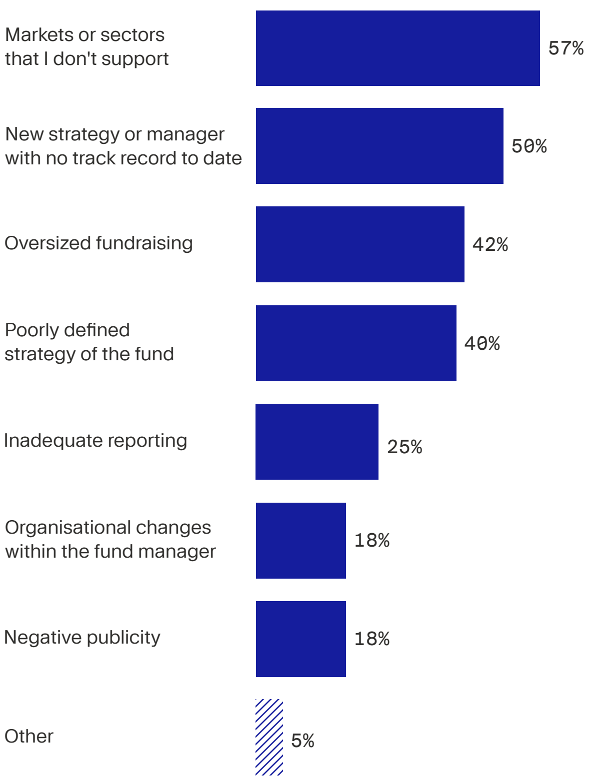
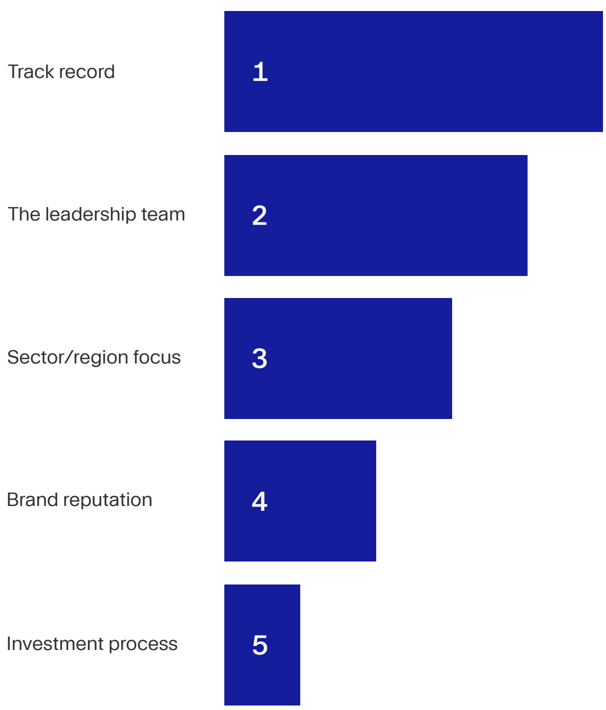


Figure 10: Funds' track record and leadership matter the most

Rank the following factors when deciding which fund manager to invest with, from most (1) to least (5) important.



Using *private equity* to *leave a legacy*

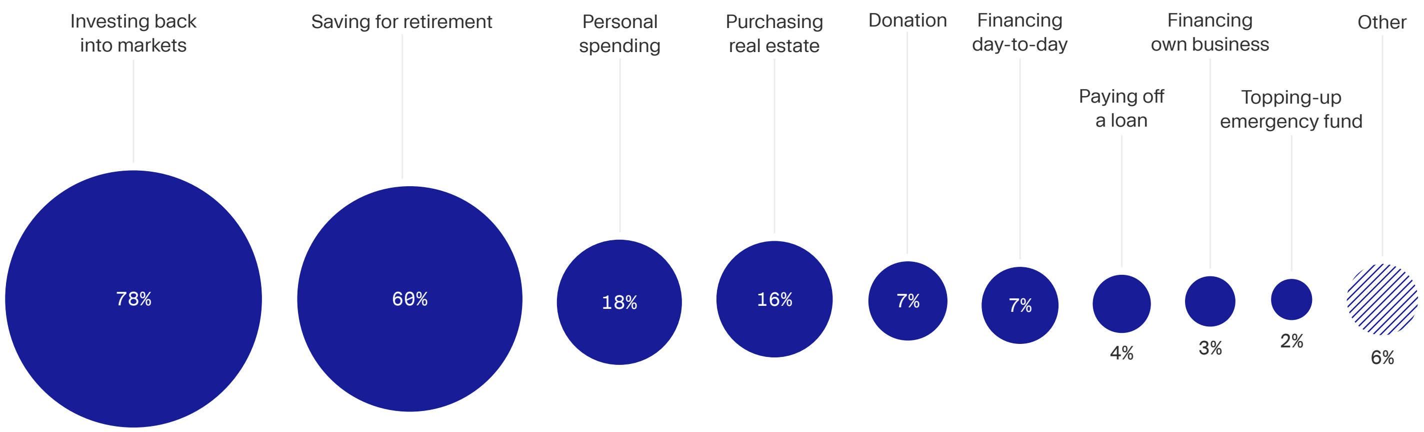
The survey showed that individual investors are drawn to private equity because of its remarkable track record and potential. But behind this simple explanation, there's a universe of personal motives.

For most, private equity is a way to further increase wealth by rerouting profits back into markets (figure 11). Some will use the money to buy property, pay off a loan or simply finance their day-to-day or larger purchases. Many people, around 60 percent according to our survey, are planning to use the proceeds for retirement, perhaps even an early one. Not a bad idea – a substantial, guaranteed cheque coming in every month for the rest of your life will probably make you happier.[34] Studies show you may live longer because of it, too.[35]

Some survey participants added their own answers. One investor said they intend to use the money to pay for school fees. Another one wants to build wealth for future generations and someone wrote "legacy". And this goes straight to what Moonfare is committed to do – helping our community to leave a legacy by accessing expert knowledge and exclusive investment opportunities.

Figure 11: Diversity of routes to spend private equity profits

How do you use or intend to use the proceeds from private equity investments? Select answers that apply to you.



Endnotes

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To learn more about opportunities to invest in funds on Moonfare's platform, please contact our team or your dedicated relationship manager.

Please note that for regulatory reasons, Moonfare is only permitted to share specific investment opportunities with qualified users after they have registered with Moonfare.

To get started as an investor, please create an account and complete your profile.

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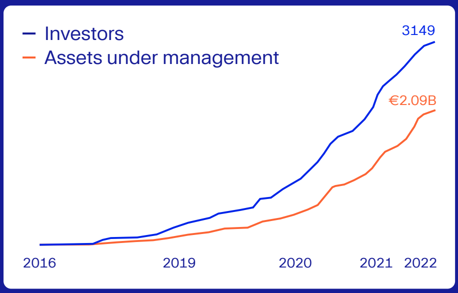

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