Private equity outlook – 2024

A year ago, we wrote that our five key predictions for the Private Equity industry in 2023 were 1. amounts raised in private equity will be substantially down, 2. 2023 will be a buyers' market for private equity secondaries, 3. "GP-led continuation vehicles" would attract increased scrutiny from regulators and LPs, 4. private equity valuations will come down and 5. Healthcare and technology investments will continue to grow. Well, this turned out to be pretty much on the mark with one caveat: valuations have indeed come down but perhaps not as much as we had anticipated.

Building on this decent inaugural effort, in a world that is facing significant global geopolitical uncertainties and 2024 being a major election year throughout the world, what does our crystal ball tell us for the next 12 months:

1. *Slow market recovery:* the fear of a global recession is abating, pundits expect interest rates to stabilise and potentially come down as early as mid-2024 and inflation is finally under – better – control. The state of the economy is not a major concern for operators anymore with supply chains largely normalized and commodity prices coming down, although higher rates do continue to put pressure on free cash flows. Over the last few weeks, we have experienced a clear rebound of business activity and seen improving liquidity as traditional lenders come back to the market, particularly in the small & mid-market across the US, Europe and Asia which is where we operate. We expect this recent upward trend to continue throughout 2024 at a moderate pace;
2. *From a buyers' to a buoyant secondary market:* The secondary market definitively was a buyers' one in 2023 (and continues to be). However, volumes were below expectations with less than $70bn transacted in the first nine months of the year. Fundamentals remain very strong with a large amount of secondary capital raised over the last few months, investors still suffering from denominator effect, lenders coming back and narrowing bid & ask spreads. As a result, we expect the secondary volumes to reach $130-150bn in 2024;
3. *Alignment of Interest challenged:* The market has been awash with "innovation" recently. From "NAV financing" to "GP-led continuation vehicles", GPs have moved away from traditional M&A exits to engineered liquidity substitutes. These structured "exits", while offering liquidity for starved LPs, can undervalue companies, substantially increase risk and more generally seem to favour the interests of GPs more than LPs. At the same time, such mispriced offerings can present attractive secondary investment opportunities;
4. *Some experience fund managers will fail to raise:* Some private equity household names, especially at the larger end of the mid-market, are currently struggling to attract interest for their new fund. They have been (ab)using some of the instruments described above in a bid to increase distributions and improve IRRs but the current overallocation to private equity from institutional investors compounded by the misalignment of interest malaise that their attitude has created will further push investors away from them; and,
5. *Retail therapy:* Increased interest for private assets from retail investors is a fundamental change. Witness the multiplication of evergreen & semi liquid funds. Regulators around the world have facilitated retail access to the asset class, something we view as a very positive development. We except to see a significant increase of "retail friendly" private asset funds in 2024 and beyond.

Like last year, Flexstone Partners twelve months outlook remains cautious. However, we are upbeat about the long-term prospects of Private Equity. Afterall, the world remains overwhelmingly private and will continue to need private equity to finance it.

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