Private Markets Outlook 2023

CIO Perspectives & Allocations

The Year of the (Re)balancing Act

January 2023

CONTENTS

CIO PERSPECTIVES

2022 has been an especially challenging investing environment, with the typical 60:40 client portfolio posting some of the worst returns experienced in decades.

Alexis Weber

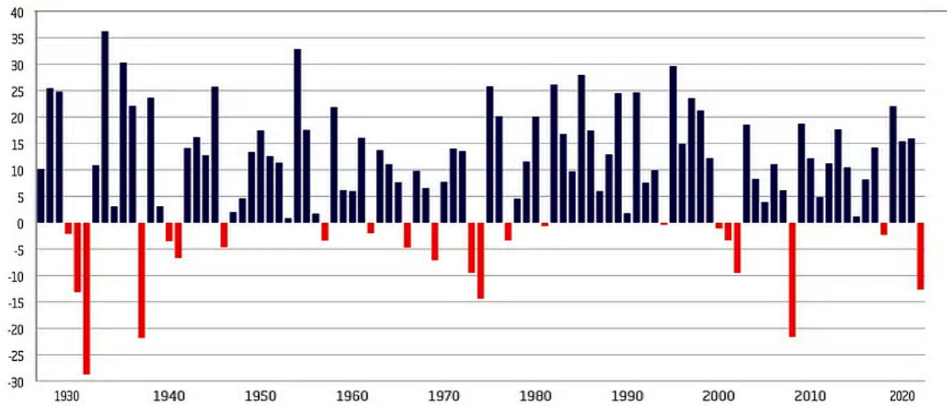
PM Alpha
CIO & Founder

In our first CIO Private Markets Perspectives & Allocations Series, we will be discussing the year ahead from a private markets' perspective in the context of the current macro environment.

With inflation at levels not seen since the 1970s, rising rates, Europe in recession and the US likely to follow shortly, we believe there is more uncertainty and volatility in the public markets to come, with the risks being very much to the downside.

> As a private markets business that focuses on wealth and asset managers, we are tasked to find solutions to the current investment challenges, laid bare in public markets investors' portfolios.
>
> Our (re)balancing act is intended to pivot portfolios towards longer-dated investments, specifically concentrated on the core macro drivers impacting portfolios today and balancing them with the fundamental secular trends that we believe will be driving growth beyond the current period of market volatility.

2022 Portfolios have been on their most catastrophic run for investors, one of the most dismal performances since 1926. With ever increasing recessionary risks following on from Europe and now North America coupled with the concerning inflationary pressures globally, we believe a major (re)balancing act would benefit Investors' portfolios.



SOURCE: Bloomberg Barclays Indices. Ned Davis Research, Inc., S&P Dow Jones Indices

Our Core Macro Drivers in 2023

1.The Great Correction

- Dislocations from assets repricing
- Corporate financing drying up
- Consumer expenditure retracing

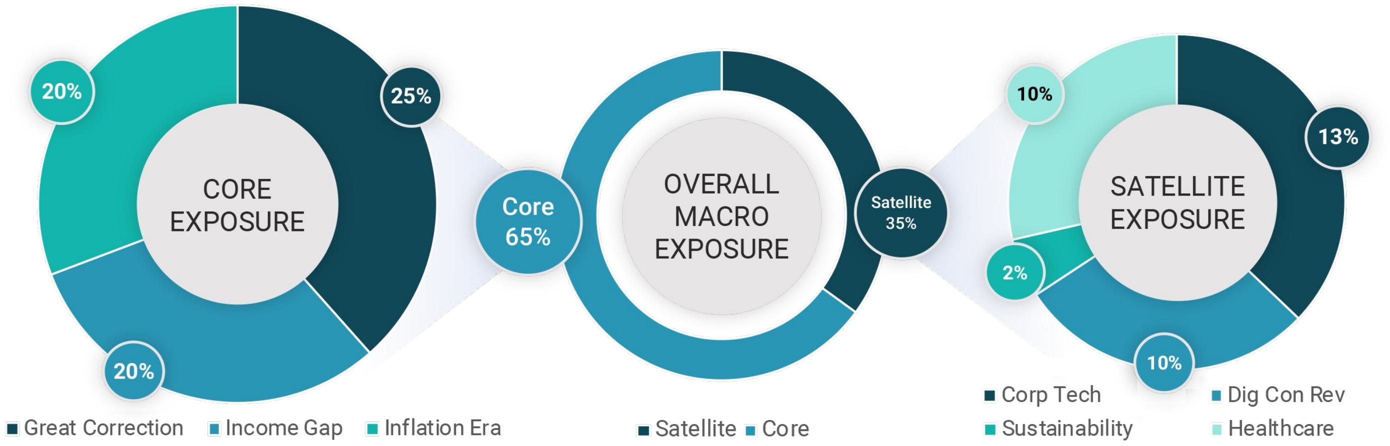
2. Inflation Era

- Higher inflation risk
- Increased cost of capital
- Shifts in monetary policy
- Consumer liquidity squeeze
- Rising energy costs

3. Income Gap

- Search for compelling yield
- Protecting from inflation
- Alternative sources of yield

PM ALPHA CIO PRIVATE MARKETS MODEL PORTFOLIO ALLOCATION FOR 2023



KEY TAKEAWAYS

Given that the macro environment continues to be uncertain and public markets likely to remain volatile over the coming few quarters, our key takeaways of this (re)balancing act for client portfolios are:

1. **Remain exposed across macro trends** like income generation and inflation protection whilst participating in secular trends across areas of corporate technology, consumer digitalization and energy transition.

2. **Benefit from the opportunity of the repricing of assets** across sectors in the next 24-36 months, making this an optimal entry point for investors.

3. **Hedge short-term volatility and risks** to the downside whilst rebalancing portfolios towards longer dated, higher yielding investments, and secular themes positioned to power the market recovery anticipated across main markets on the backend of 2023, early 2024.

> “Private markets are the ideal stage for executing on a targeted investment strategy. The fact that the vast majority of economic activity and commercial revenues are generated by private companies means the opportunity set for investors is orders of magnitude greater than those offered by public markets.”

Tom Douie, CEO, PM Alpha

PRIVATE MARKETS ALPHA

For more details, register for our platform at **www.pmalpha.co.uk** and visit the Alpha Insights section.

RECESSIONARY RISKS, DISLOCATIONS AHEAD

As investors navigate an unprecedented market regime, we see private market investments as a core solution for portfolios. Private assets continue to attract capital as investors seek better returns. We think private markets can continue to deliver for investors, but will increasingly rely on hard-to-access areas and specialist skills.

Private Markets demonstrated their ability to navigate volatile periods during the Global Financial Crisis in 08/09 and did again throughout the Covid-19 crisis, while global stock markets and 60/40 portfolios corrected by more than 20% in Q1 2020. Private markets are well-suited to this type of backdrop, given a broad range of different return drivers, which can create value in a variety of ways that we will touch on later. This is especially important in an environment of increasing interest rates which is likely to remain the case for some time.

We believe this is being reflected through investors' increasing risk aversion. Portfolios are being rebalanced to more defensive positioning, with only some selective opportunistic buying of cheaper assets, as assessed on a risk-adjusted basis.

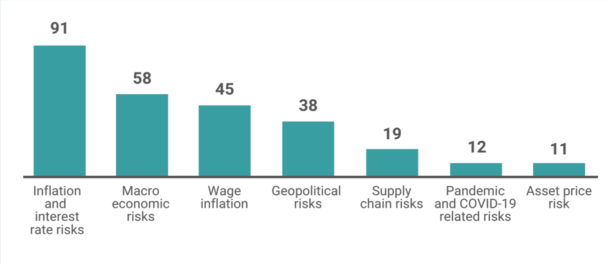
Global GDP Growth

Annual Change (%)

SOURCE: IMF

Most Important Macro Factors

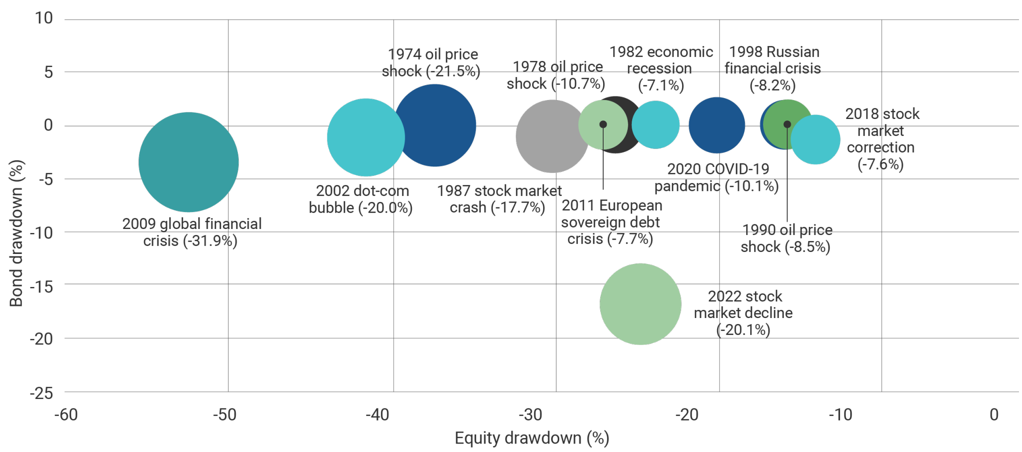
Investors consider these factors to be among the top 3 risks (%)



SOURCE: BCG

We are also seeing a growing desire to see through current market uncertainties and attempt to anchor today's portfolios with longer term investment themes that will ultimately weather the storm and potentially lead an eventual market recovery.

We think this tumultuous environment will cause investors to rethink portfolio construction and look to medium and long-term opportunities. Private markets investments are one means of accessing these, but as we know, not always available to all clients' portfolios.



SOURCE: Bloomberg, Barclays Private Bank, October 2022

PRIVATE MARKETS – A KEY FOR INVESTORS IN TURBULENT TIMES

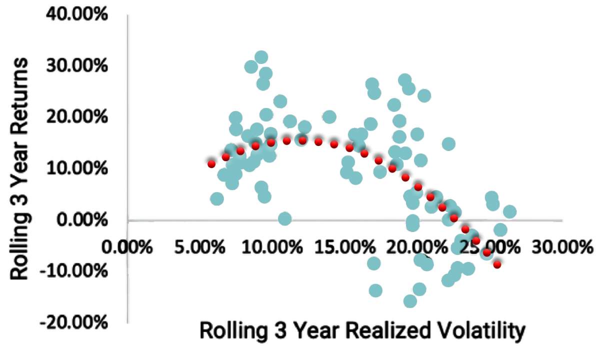
There are some specific characteristics of private markets that make them an attractive portfolio tool, especially during uncertain macro-economic conditions:

1. Private markets are much larger than public markets meaning that the **breadth of available opportunities** are therefore greater.

2. It can be clearly demonstrated that allocating to **private markets at times of recession and public market volatility leads to some of the best investment returns** that private markets have to offer.

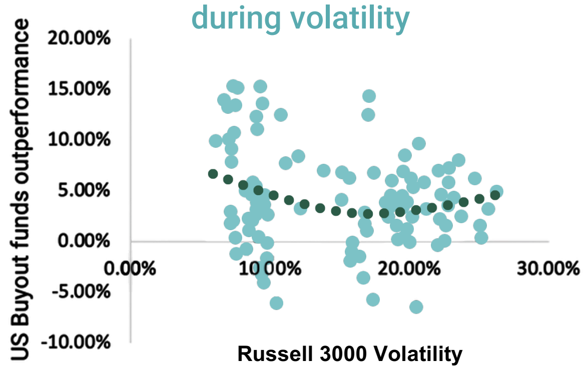
3. As committed capital is spent by private markets managers more gradually and is locked up for a period of time, it increases the ability of those managers to **exploit market dislocations and select the best potential growth opportunities.**

Public markets during volatility



SOURCE: Hamilton Lane Data via Cobalt, Bloomberg (September 2018)

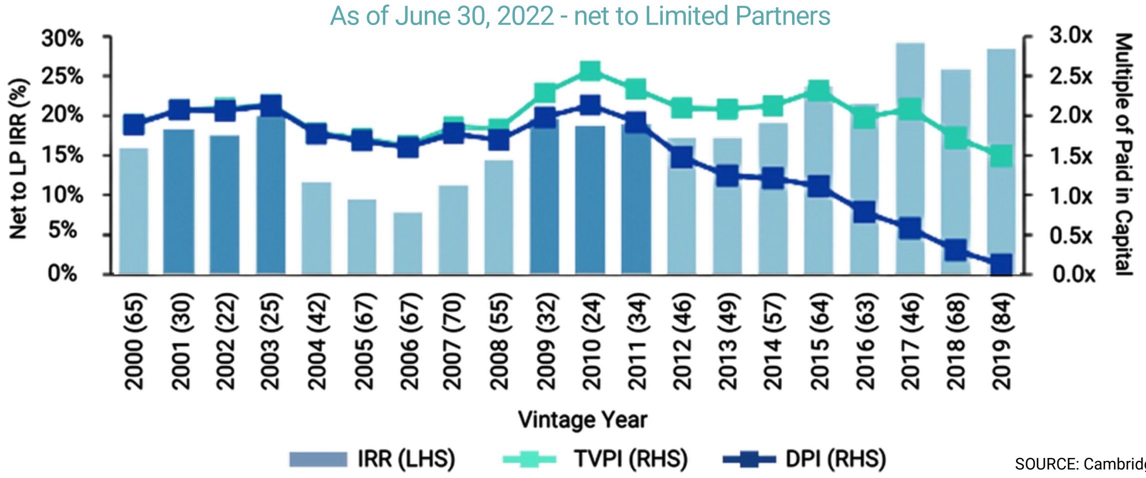
Private market outperformance during volatility



SOURCE: Hamilton Lane Data via Cobalt, Bloomberg (September 2018)

Recession era vintages have shown resilience

As of June 30, 2022 - net to Limited Partners



SOURCE: Cambridge Associates

FACING CHALLENGES AHEAD: REBALANCING ACT

Optimal Private Markets' Allocation 2023:

Conservative Profile	Balanced Profile	Growth Profile

10% — 20% — 40% — 60%

PM Alpha recommends 10-60% Portfolio Allocation to Private Markets

Core Macro Drivers:

65%

The Great Correction	Inflation Era	Income Gap
25%	20%	20%

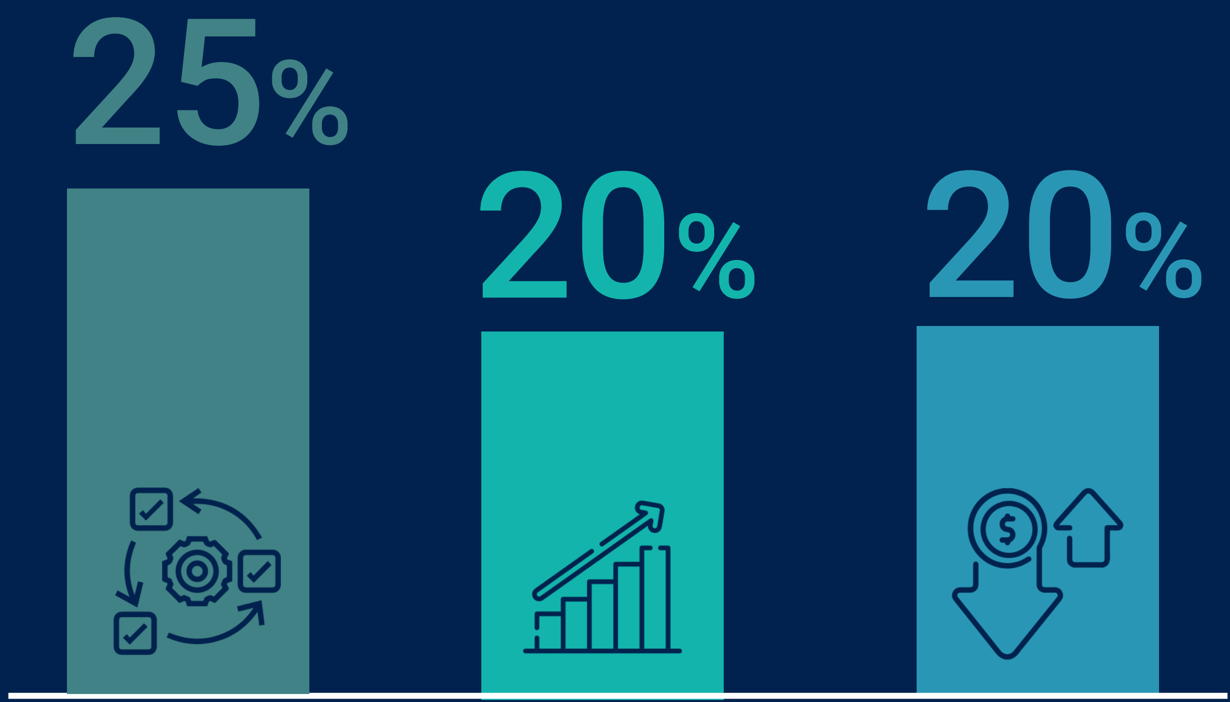
Satellite Secular Trends:

35%

Corporate Tech	Healthcare	Digital Consumer	Sustainability
13%	10%	10%	2%

Private markets investments serve as an instrumental portfolio tool in this rebalancing act. By increasing or adjusting allocations to the various underlying strategies, asset classes and instruments that provide exposure to these core macro drivers and satellite secular trends, portfolios can be repositioned for resilience and growth through this market cycle and beyond.

OUR TOP 3 MACRO DRIVERS



1.The Great Correction

Value in dislocations emanating from the repricing of global assets

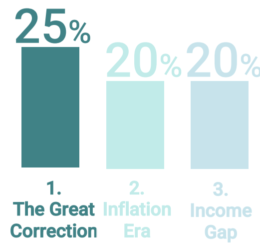
2. Inflation Era

Turning Inflationary Challenges into Opportunities

3. Income Gap

Searching for Alternative Sources of Yield

OUR TOP 3 MACRO DRIVERS



1. THE GREAT CORRECTION

Value in dislocations emanating from the repricing of global assets

After a prolonged leveraged era powered by artificially suppressed interest rates, the return to pre-GFC economic norms will likely be accompanied by a strong period of dislocations, driven by the increasing debt-wall faced by governments, corporates and consumers.

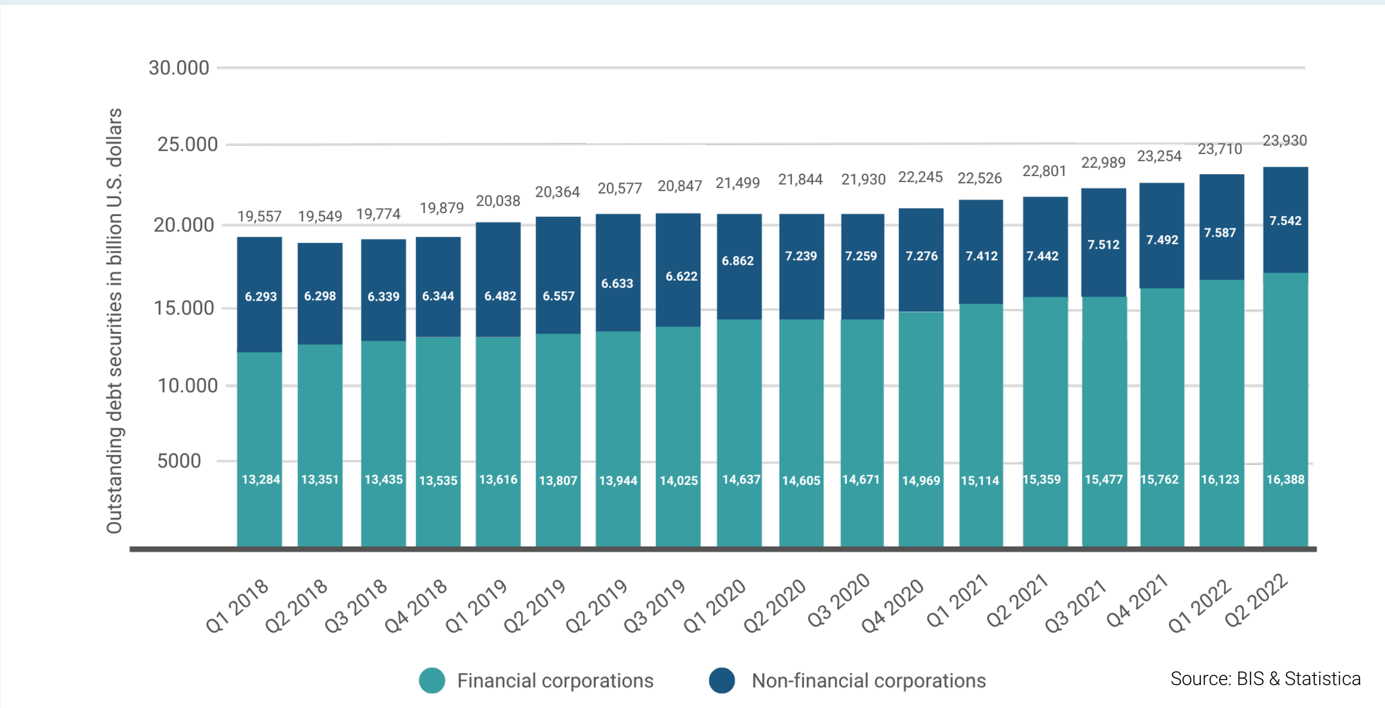
When coupled with high inflation and a recessionary environment, the inevitable interest rate hikes produce devastating dislocations and distress across most sectors and asset classes, and negatively impacts consumer expenditure.

In this difficult operating environment, some companies will do a better job than others of anticipating revenue and earnings volatility and will ensure a medium-term refinancing package (often in private markets) meeting their specific needs during this volatile phase. With corporate financing drying up and the debt wall outstanding continuing to expand, there is likely to be an increased wave of restructurings causing balance sheet dislocations and distress in the near future.

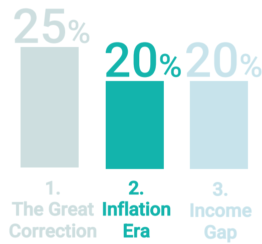
This will provide opportunities for selective investors to unlock value-trades in this repricing of assets and benefit from their repositioning towards the medium-term recovery.

Outstanding Value Of Corporate Debt Securities In US

From Q1 2008 - Q2 2022, By Corporate Type (in Billion U.S. Dollars)



OUR TOP 3 MACRO DRIVERS



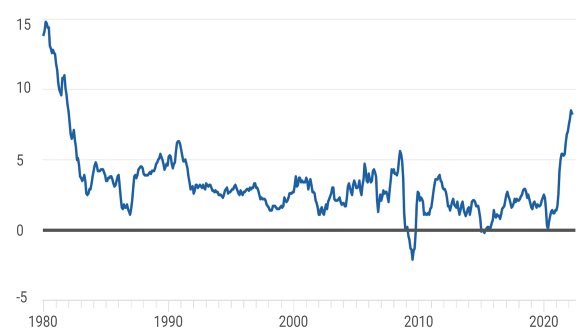
2. INFLATION ERA

Positioning Portfolios for a Prolonged Era of Inflation

Inflation will profoundly impact portfolios over the longer term, and it is therefore crucial to reposition these towards longer dated assets that can generate positive real yields and growing cash-flows to counteract inflationary pressures.

US Inflation Figures

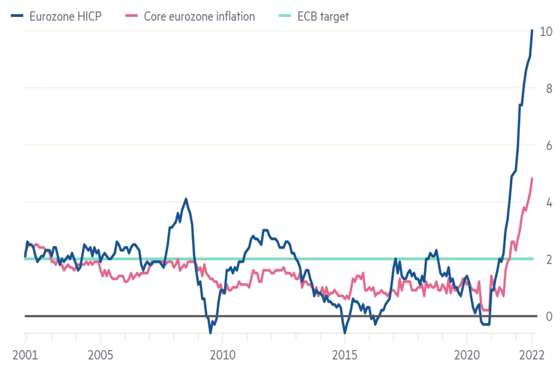
Consumer Price Index
(Annual % change)



Source: Refinitv/FT

Eurozone Inflation Figures

Harmonised Index of Consumer Prices
(Annual % change)

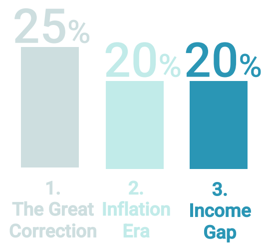


Source: FT

Recent monetary and fiscal stimulus as part of the governments' response to inflationary pressures, is in our view, an underestimated risk. Inflation may surprise on the high side for longer, even if the actual year-over-year inflation numbers peaked in 2022. Certain structural forces could keep inflation higher – including significant shifts in the monetary policy of major central banks, a changing labour force and the ongoing deglobalisation of trade and energy.

Finding Opportunities Ahead

As investors look to turn inflationary challenges into opportunities, we consider including **real assets, private credit and infrastructure** due to its more defensive and medium-term CPI-linked cashflow characteristics. Rising inflation and interest rates effectively raise the cost of capital across long-term leases for real estate and infrastructure assets; however, real estate and infrastructure have naturally protective inflation hedges. Infrastructure such as transportation and logistics remain essential in times of economic stress as countries continue to use, build and consume infrastructure services.



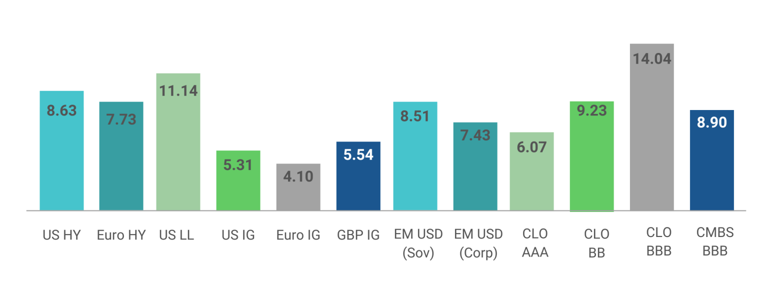
3. THE INCOME GAP

Solving the Gap through Alternative Sources of Yield

Although yields have been rising of late, investors starved of compelling, durable income will continue to look at private markets as a reliant source of income. In addition, the search for yield must now be coupled with a need to protect against inflationary trends. There are some strategies within private markets that carry an inherent inflation hedge, and some that are poised to benefit from rising inflation.

Credit Yields have Retraced Higher In 2022

As of November 2022



Source: Bloomberg Index Services Limited, Credit Suisse, and J.P.Morgan Securities

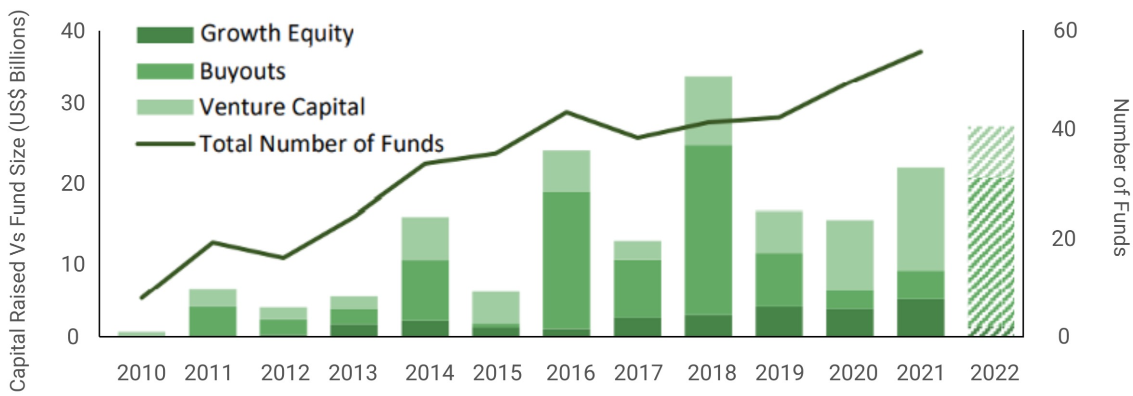
We also expect that the secondaries market will continue to see increased levels of activity. As the broader financial markets struggle with current recessionary dynamics and the repricing of late-cycle valuations, ample opportunities will emerge for secondary investors to acquire deals at a discount.

Alternative Credit has proved its ability to deliver a durable premium through the economic shock caused by the pandemic, as well as other dislocations, over the past decade. Higher yields attainable in the private debt markets have offered premiums, whilst maintaining the same seniority, collateral and protection packages, above those in the high-yield and leveraged loan markets.

Investors can also turn to middle-market corporate borrowers across diverse industries, speciality finance strategies, as well as alternative loans to middle-market companies for additional sources of yield.

Capital raised by US Private Diverse Managers has increased over time

2010 - 2022 (Data for 2022 are as of October 10)

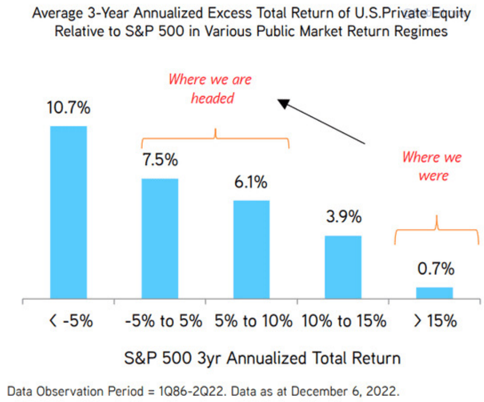


SOURCE: Cambridge Associates LLC.

PRIVATE MARKETS – LONG TERM VALUE CREATION

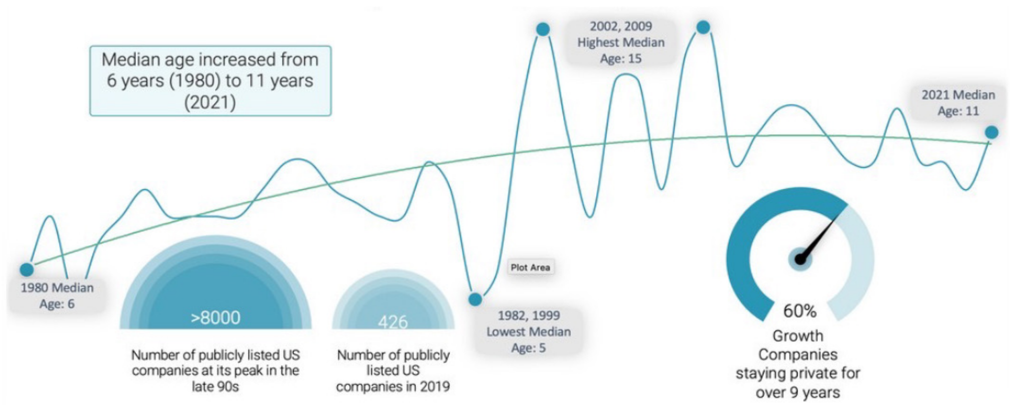
As companies stay private for longer, the breadth of opportunity for specialists private markets managers to generate value over the medium to long term continuously expands. This is especially the case during volatile market conditions, where the premium generated by private investments has been historically higher than during stronger markets.

The value of the illiquidity premium tends to go up in bumpy markets



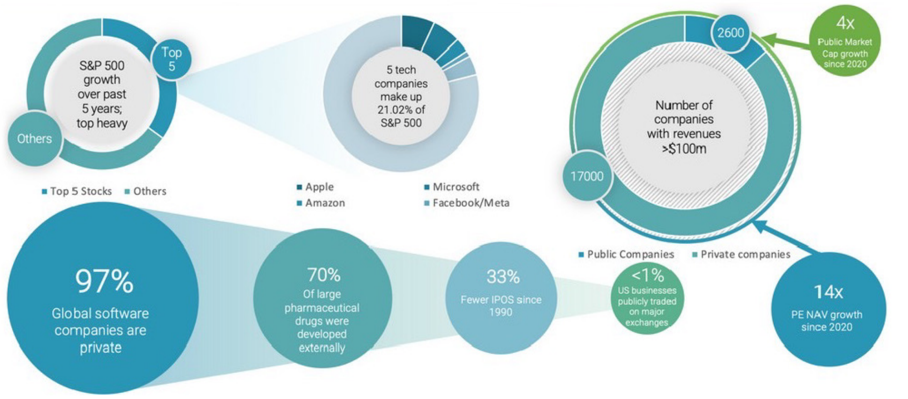
SOURCE: Cambridge Associates, S&P, KKR Global Macro & Asset Allocation analysis

Companies are Staying Private for Longer…



SOURCE: PM Alpha

…A Greater Proportion of Value Creation is Happening Pre-IPO



SOURCE: PM Alpha

THE FINAL ACT: FOCUSING ON SECULAR TRENDS

The “final act” is focused on concentrating allocations across the most prevalent strategies, offering access to the breadth of sectors and markets impacted by transformational secular trends.

Private markets are also well positioned to capture secular – or non-economically sensitive – trends before they are accessible through listed stock markets giving investors a medium-term lens of growth prospects across the core economic drivers.

We believe Covid-accelerated megatrends will benefit investments of this vintage across asset classes, with robust competition for assets, making deal sourcing and selection increasingly important. As the private markets have developed, they have increasingly become an important source of capital when compared to public markets. Companies are now choosing whether to go public or private for their financing needs.

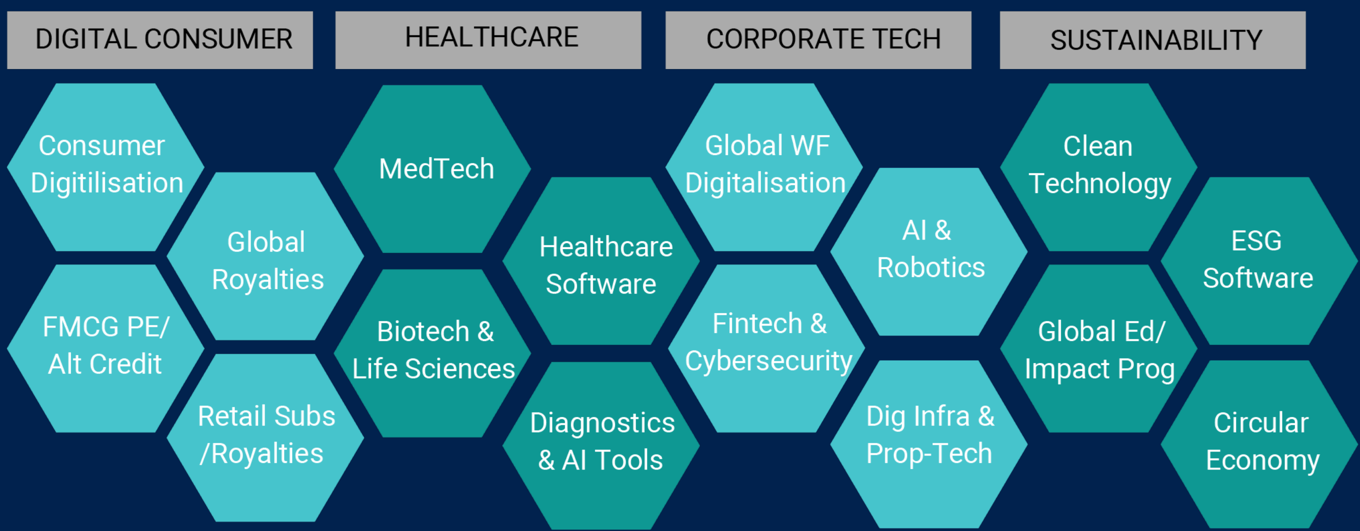
The world is moving at very different speeds in terms of demographics and growth. The breadth and depth of private markets explains why their presence is ever increasing in investors’ portfolios from institutional, asset and wealth managers, to individual HNW investors. Private markets naturally offer the investor significant illiquidity premiums over public markets. This needs to be carefully diversified across different asset classes, strategies, vintages, geographies and investment instruments. A private markets solution that utilises multiple managers, funds and ultimately underlying asset holdings reduces the impact of any defaults in underlying portfolios on the collection of structural illiquidity premiums.

1 The Corporate Tech Revolution

2 Healthcare Everywhere & for All

3 The Maturing Digital Consumer

4 Achieving the Sustainability Path through the Re-localisation of Trade



1. THE CORPORATE TECHNOLOGY REVOLUTION

The Corporate Technology Revolution has driven adoption by a broad base of corporates, and those opportunities to finance both tech companies & the accelerated digitalisation of traditional businesses.

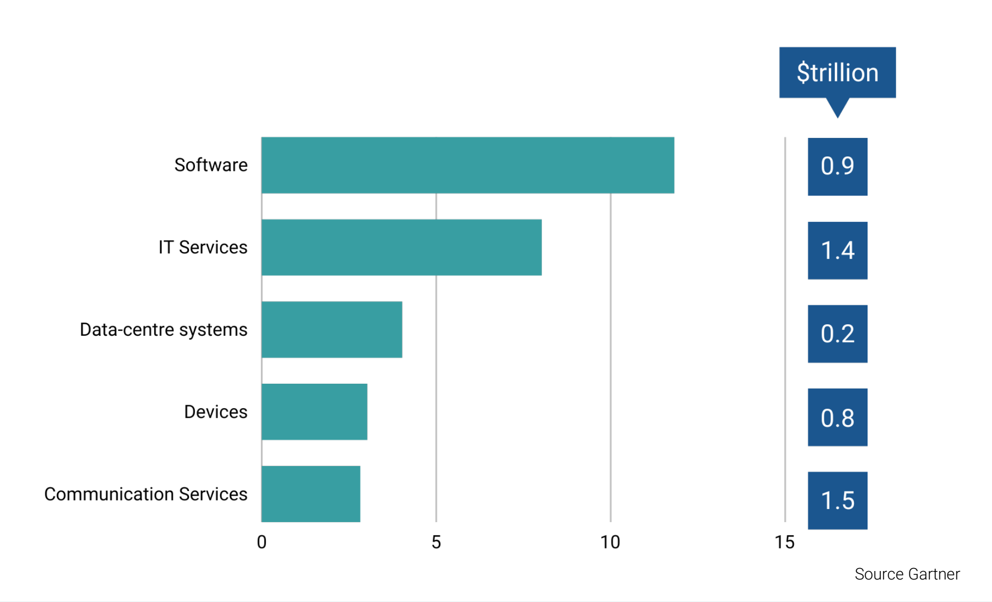
Businesses and rollup platforms need fast, flexible capital, as volatility is the enemy of rapid change, which rapidly creates winners and losers across verticals. This will be supported by a strong consolidation in the industry powered by the tech hungry buy-out powerhouses looking to deploy their wall of dry powder into these secular technology trends. **We therefore anticipate a strong waive of M&A and serial buy-build plays across all B2B technology market verticals.**

For real-asset investors, digitalisation means potential long-term revenue streams from cell towers, data centres, broadband buildouts, decentralised electrical grids and smarter customer meters.

We see considerable future demand for capital, and a strong flow of opportunities across private equity and private credit. Concerns over a slowing economic growth or an outright recession also present more challenges to the whole sector although some are more resilient, e.g. data centres & warehousing. We also see opportunities from accelerating structural change, especially technological disruption.

IT Spending

Global Forecast % Increase, 2022 - 2023



2. HEALTHCARE EVERYWHERE & FOR ALL

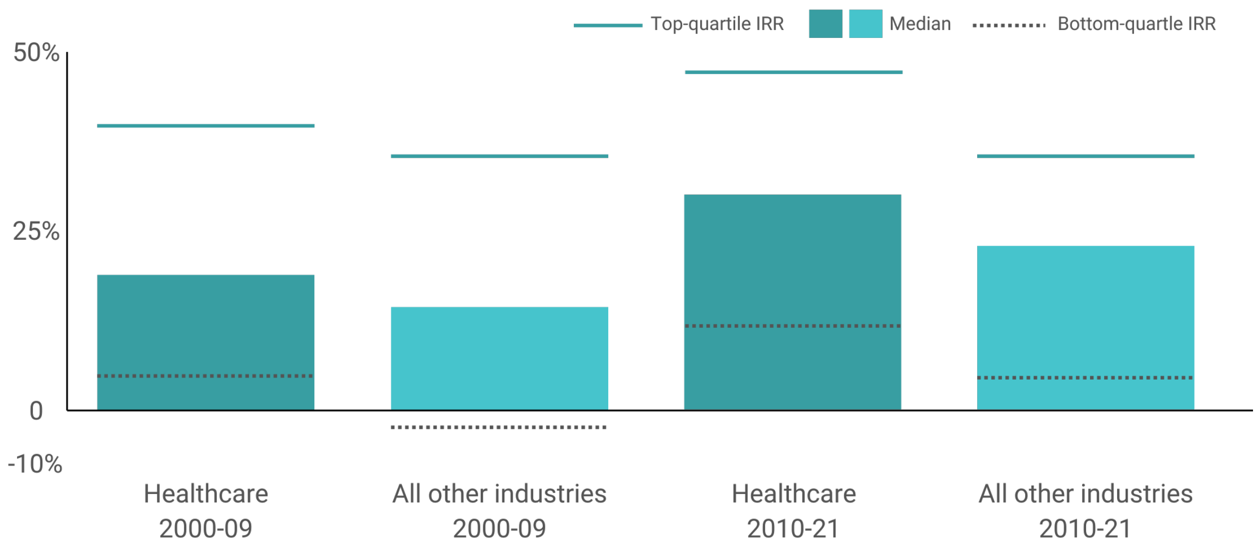
An Ageing Population & the Era of Mental Health

The profound changes undergone over the last decade, including breakthroughs in digital health, the emergence of novel therapies, the breakout of a major pandemic, the rise of personalised care, and value-based care are all fundamentally transforming the healthcare sector.

Several secular trends are continuing to benefit healthcare growth companies: an ageing population, the rising incidence of chronic illness, healthcare access in emerging markets and digital innovations in treatment and operational processes are boosting demand for an array of healthcare goods and services.

Pre-covid healthcare was an attractive growth segment. Today, the tailwinds are stronger across healthcare technology, telemedicine and beyond. In services, an ageing population and the increased focus on healthcare provision are creating core opportunities to invest across growth markets in debt and equity capital.

Improving Returns in Healthcare vs. Other Industries



Source: DealEdge

3. THE MATURING DIGITAL CONSUMER

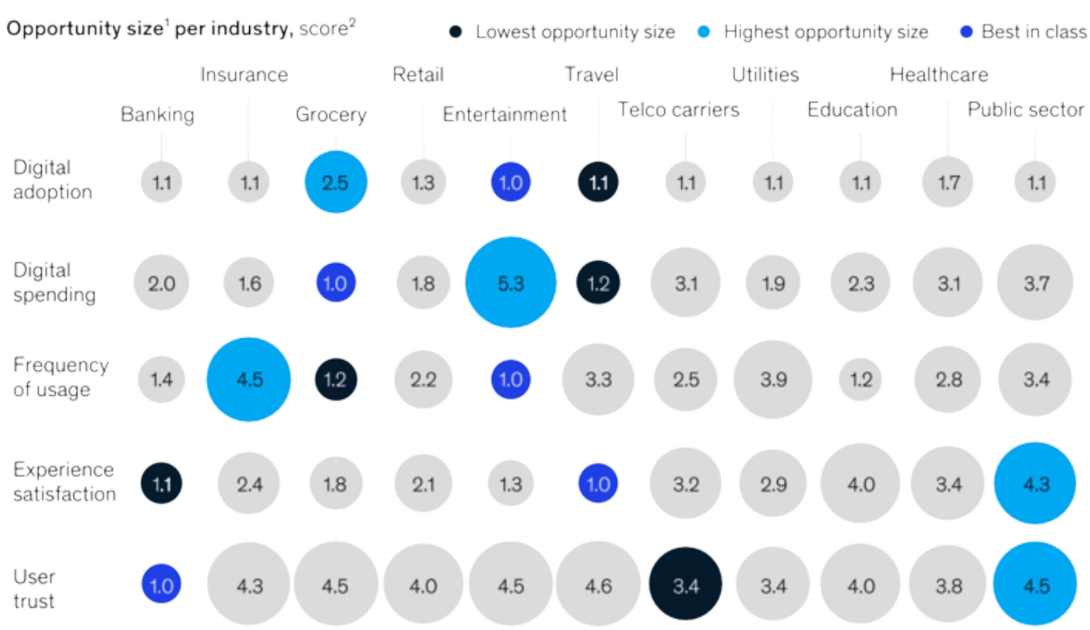
Despite rising rates and inflationary pressures that generally undermine more cyclically oriented digital services, **consumer technology spend is expected to continue its growth through these recessionary periods.**

The growth is expected to drive further adoption through the bundling of digital services distributed through customised portal services. The current 'cash squeeze' faced by consumers will result in a strong consolidation wave for their primary digital services to reach a stable price point.

The unification of services through high-speed portals can only be supported by the relevant digital infrastructure and operating services. Bundled services will drive a personalised offering which will see further penetration within consumer expenditure, and will provide consumers full interactivity and augmented reality.

In our opinion, this will drive interesting allocations across maturing technologies, digital infrastructure, digital bundled services and portal frameworks.

Companies can look outside their industries to find best-in-class opportunities



Source: McKinsey

[1] Survey Questions related to participants usage and satisfaction with each industry

[2] Reflects opportunity to improve relative to best in class, in a given dimension, calculated as maximum value per dimension, divided by industry value, with values

4. ACHIEVING THE SUSTAINABILITY PATH

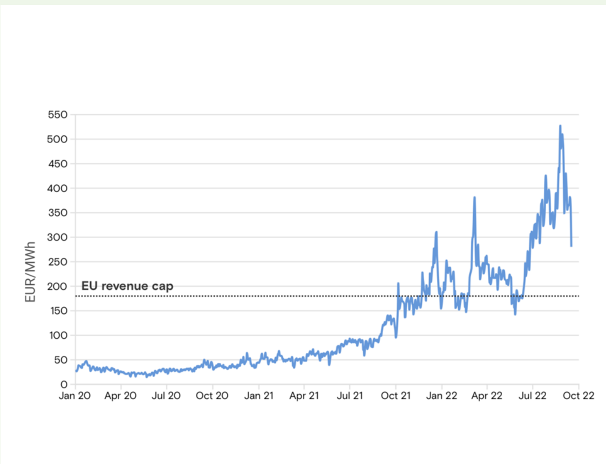
– through the re-localisation of trade

We believe that local and shorter logistical frameworks will help us reach a more sustainable path over time. One way is through energy efficiency. With energy and fossil-fuel prices continuing to soar and as many nations aim to reach Net Zero by 2030, we believe the path to energy transition will remain at the forefront of investors' minds. **Exit opportunities for longer-dated closed end private markets funds holding clean energy assets over this period could become highly favourable.**

Partnering with specialist private market managers deploying capital in these opportunities could unlock long-term value for investors. In addition to clean energy investments, we like opportunities in diverse technologies across the food value chain and those supporting climate change mitigation.

European electricity prices rose sharply in 2022

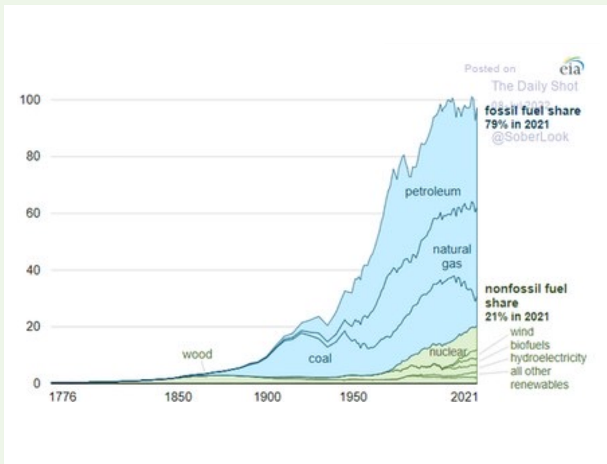
Mean wholesale electricity price across EMU-4 (France, Germany, Italy, UK) and The Netherlands



Source Goldman Sachs Research

Energy consumption in the United States (1776 - 2021)

Quadrillion British thermal units



Source Goldman Sachs Research

INVESTMENT THEMES

Core Allocations

25% THE GREAT CORRECTION

UK £ Dislocation	5%
EU/NAM Secondaries (VC Growth PE)	20%
Real Assets Dislocations	25%
Global Distress	50%

20% INFLATION ERA

FMCG Special Situations	5%
Core Real Estate & Build-to-Rent	15%
Transportation & Logistics	30%
Infrastructure Alternatives	50%

20% INCOME GAP

Diversified Alternative Income (Royalties/GP Stakes)	20%
Mid Market Corporate Credit	30%
Global Secondaries	50%

Satellite Allocations

13% CORPORATE TECH

Global Workforce Digitalisation	50%
Digital Infrastructure & Prop-Tech	30%
Fintech & Cybersecurity	10%
Semiconduct., AI & Robotics	10%

10% HEALTHCARE

MedTech	40%
Biotech & Life Sciences Platforms	20%
Healthcare Software & IT	20%
Diagnostics & AI Tools	20%

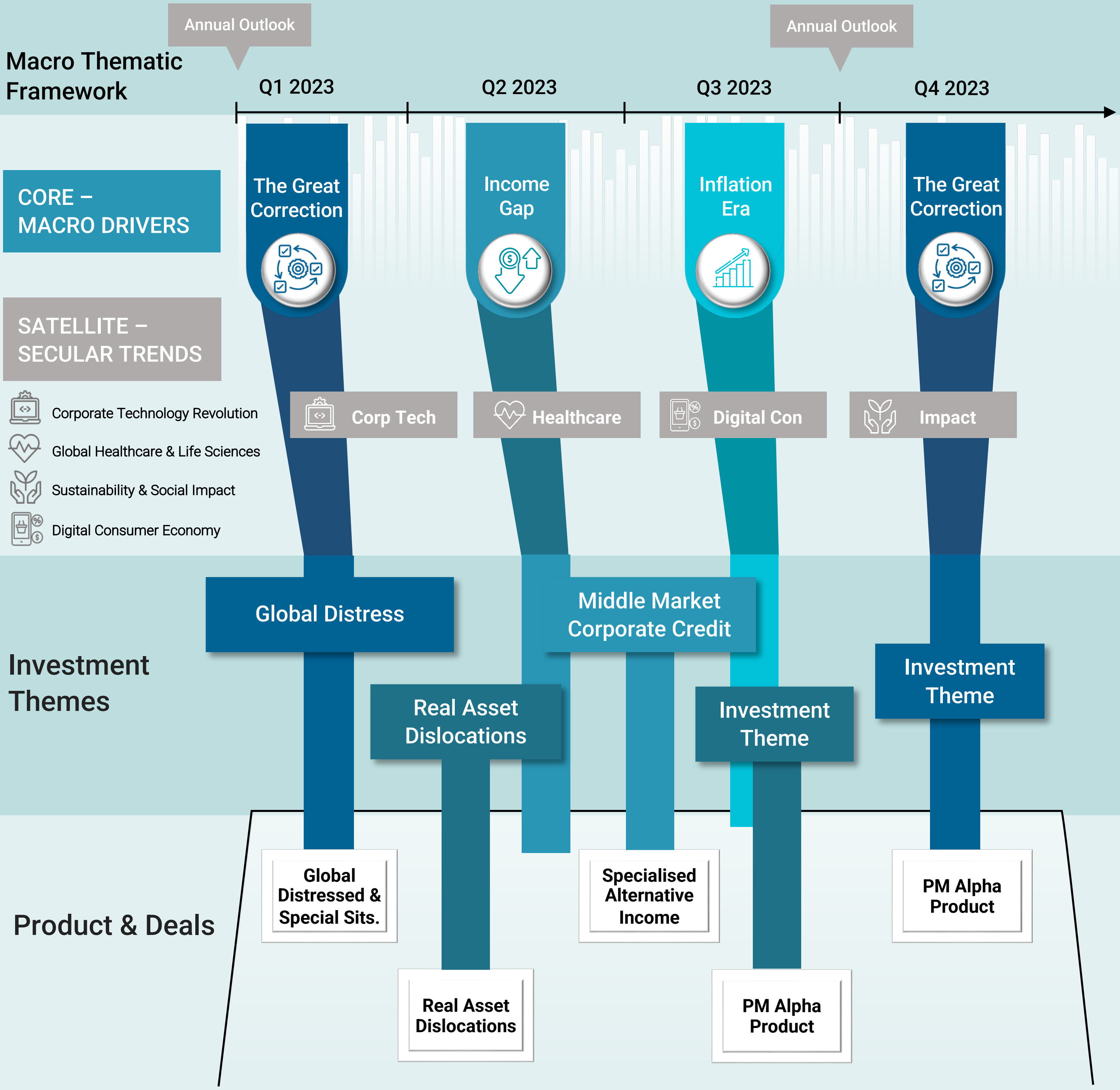
10% DIGITAL CONSUMER

Consumer Digitalisation	40%
FMCG Private Equity/Alt Credit	20%
Global Royalties	20%
Retail Digital Subscriptions/ Royalties	20%

2% SUSTAINABILITY

Global Education Impact Prog	40%
Clean Tech	30%
ESG Software	20%
Circular Economy	10%

PM ALPHA INVESTMENT PIPELINE



SOURCE: PM Alpha. For Illustrative Purposes. Does Not Constitute Investment Advice

PRIVATE MARKETS ALPHA

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