# Q4 2020 & Year-End Valuations

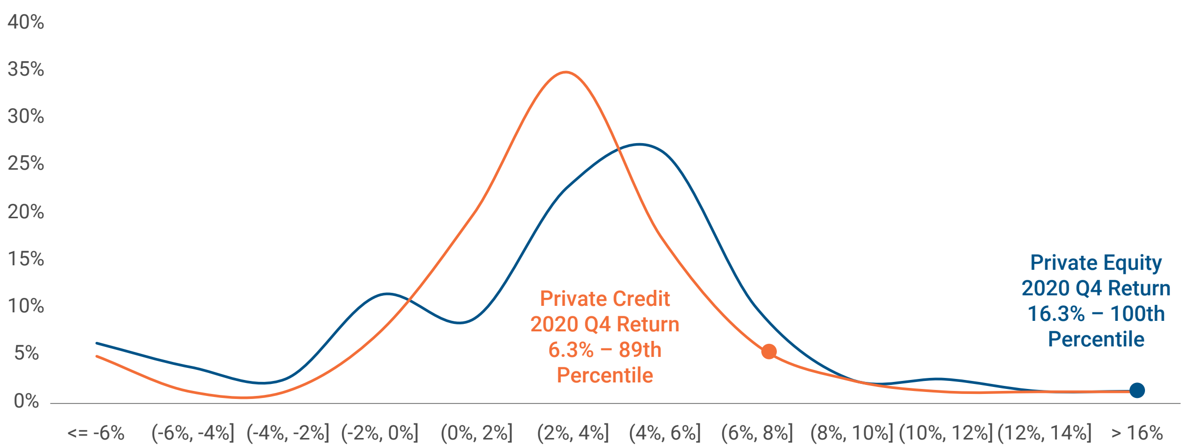
**June 17, 2021** | Bryan Jenkins, Head of Private Market Analytics

## The whipsawing observed in listed markets over the course of 2020 made for some of the most eagerly anticipated year-end private markets valuations in recent memory.

Readers of our COVID-19 & Market Updates will recall that we've been predicting for some time that Q4 2020 would be one of the best quarters for private markets in recent memory, with the caveat that it would also show the widest dispersion of returns between funds. We also posited that calendar year 2020 would show similar record levels of dispersion. It's time to check our work and examine how those predictions fared.

Let's start with the headline performance numbers for Q4 2020. Private equity strategies returned 16.3% over the course of Q4 2020, while private credit strategies returned 6.3%. Those returns are among the best single quarter returns in the last 20 years:

**Private Equity & Private Credit Quarterly TWR Distributions**
Trailing 20 Years

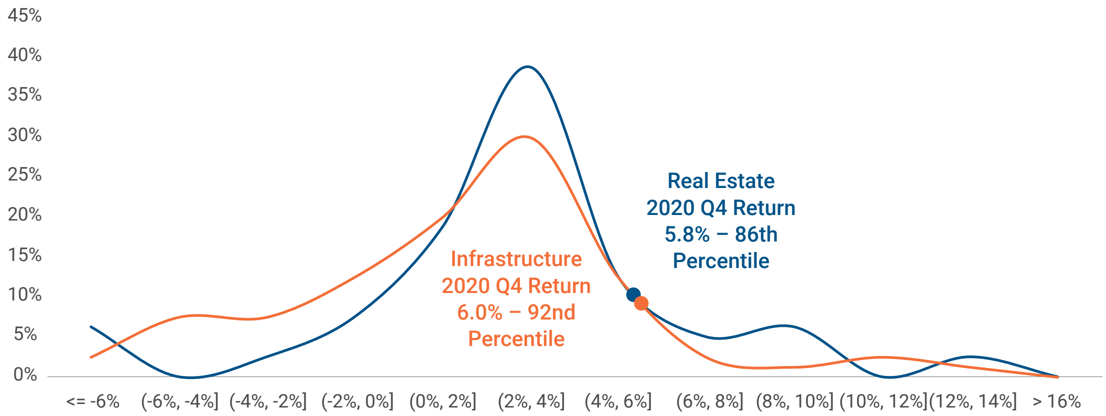



Source: Hamilton Lane Data via Cobalt (June 2021)

How about real assets? Much like private equity and private credit, real estate and infrastructure also fared very well relative to historical averages:

**Private Real Estate & Private Infrastructure Quarterly TWR Distributions**

**Trailing 20 Years**



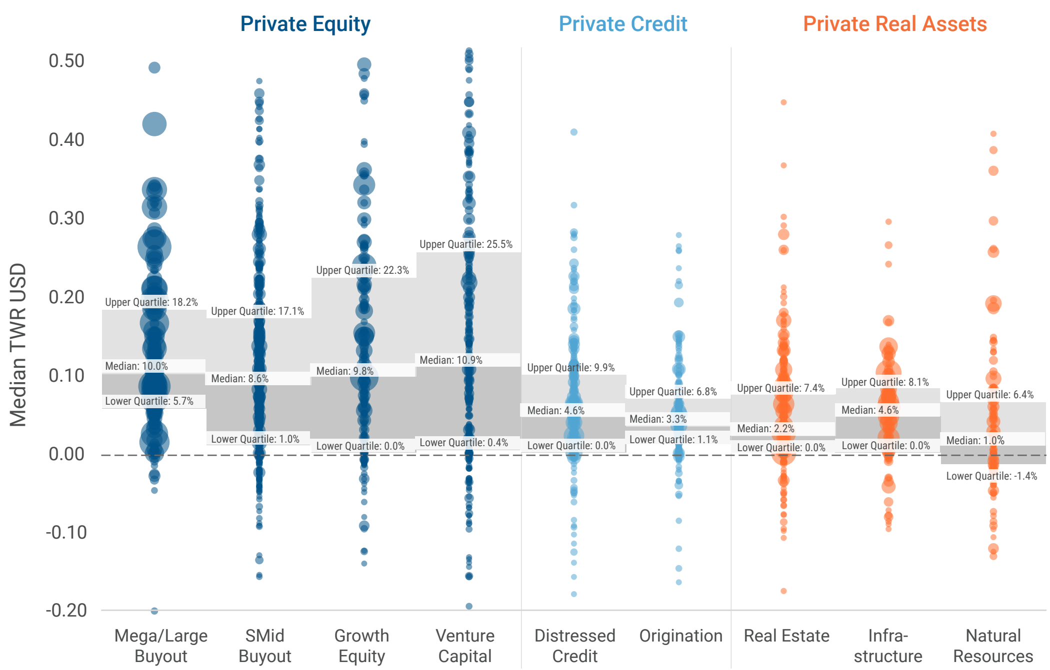

Source: Hamilton Lane data via Cobalt (June 2021)

So, our prediction of Q4 being one of the strongest quarters in recent memory seems to hold, though admittedly it was not a particularly bold or uncommon prediction. What about our second prediction about increased dispersion at the fund level?

We've shown a version of the chart below in earlier market updates. Each dot represents the Q4 2020 return of fund in the respective strategy. We've overlayed quartiles on each strategy to get a sense of the summary distribution statistics.

**2020 Q4 Private Markets Fund Return Distribution**

**By Strategy, Vintage Years 2010-2020**




Source: Hamilton Lane Data (June 2021)

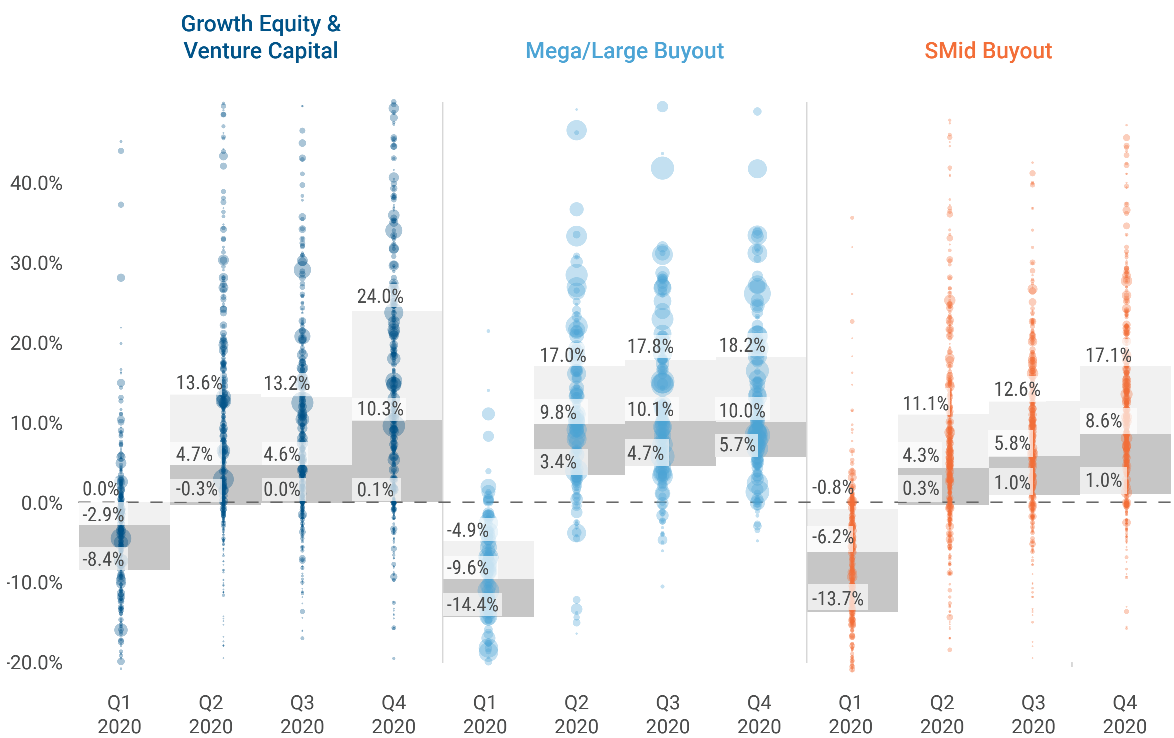
Bubbles sized by NAV. Y-axis is truncated for visibility. Some individual data ponts may not be visible.

A few things stick out to us:

- As you might expect, the dispersion of returns in Q4 2020 was higher among strategies with higher perceived risk. Origination credit and infrastructure had relatively narrow dispersion, while growth equity and venture capital experienced the most.
- The 3rd / 4th quartile boundary was close to 0% for most strategies, implying there were still ~25% of funds that took a markdown in Q4. The notable exception to this rule was mega / large buyout, with a 3rd / 4th quartile boundary closer to 6%.
- Larger buyout funds outpaced their smaller peers on a pooled and median basis in Q4, with a higher top quartile hurdle and a higher bottom quartile threshold – which also held true for prior quarters in 2020. Is this a case of larger buyout funds showing more sensitivity to short-term market movements, or is it perhaps indicative of a longer-term trend?

**Private Markets Fund Return Distribution by Quarter**

**By Strategy, Vintage Years 2010-2020**



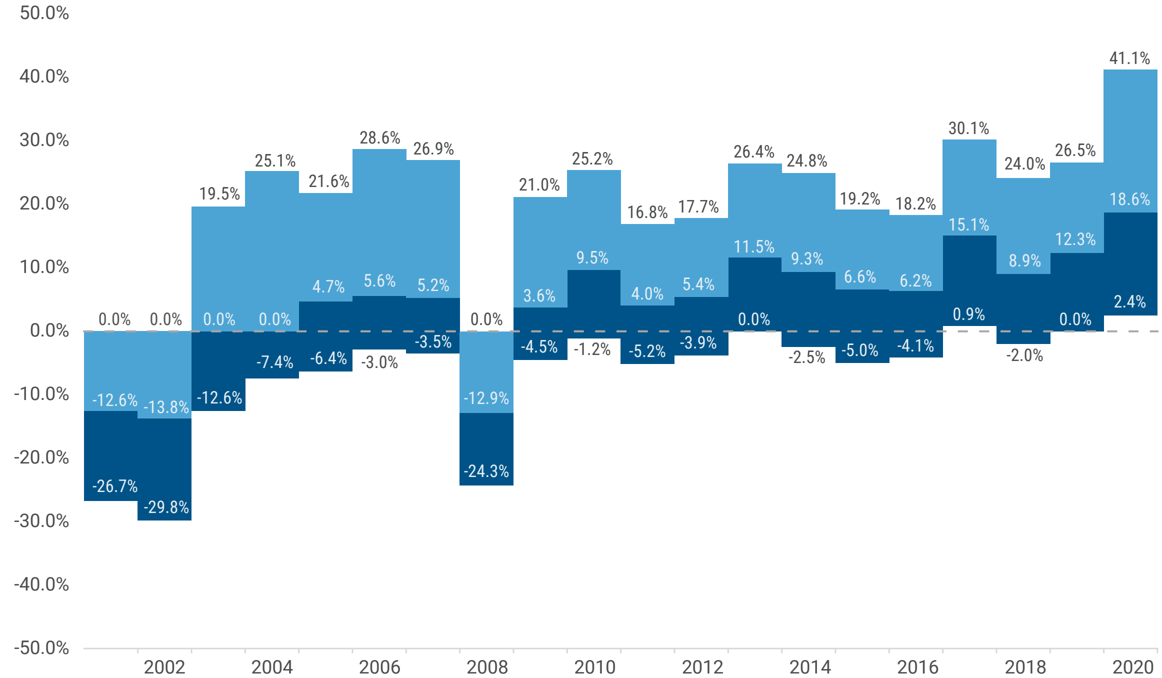

Source: Hamilton Lane Data (June 2021)

Bubbles sized by NAV. Y-axis is truncated for visibility. Some individual data ponts may not be visible.

- We sifted through the top quartile performers to see if there were any common threads , but surprisingly, there weren't any immediately obvious links among them. Funds of all sizes, regions, and sectors – even funds investing in hard hit sectors like hospitality – performed well in Q4.

What about on a calendar year basis?

### Private Equity Spread of Calendar Year Returns

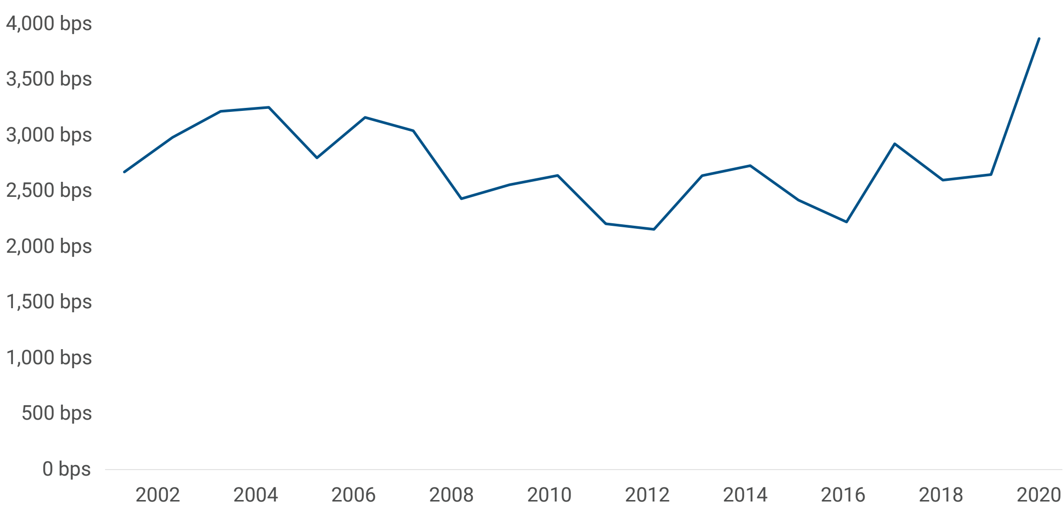



Source: Hamilton Lane Data via Cobalt (June 2021)

For the full calendar year 2020, median returns for private equity funds were the highest since the turn of the millennium, at 18.6%. While downside (measured by the bottom quartile threshold) was consistent with recent years, the upside for top funds was a lot higher: Managers would have needed to post a >40% (!) return for the year to be among the best performers. Those elements mean that dispersion of returns, measured by interquartile range, was the widest it's been in the last 20 years, bucking a two-decade long trend of moderate declines in calendar year return dispersion:

### Private Equity Calendar Year Spread of Returns

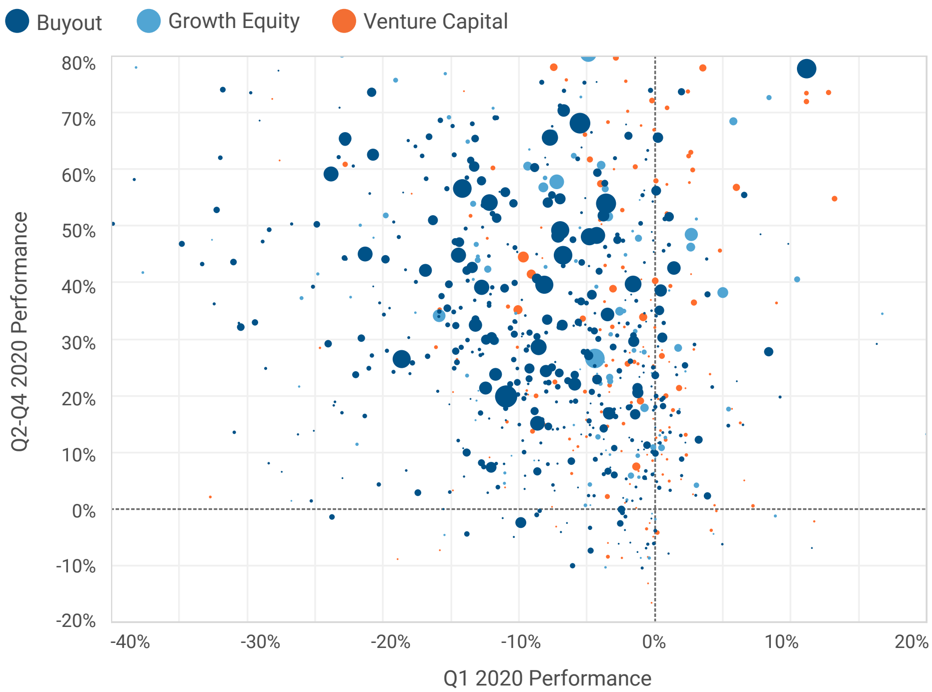
**Interquartile Range in bps**




Source: Hamilton Lane Data via Cobalt (June 2021)

In our 2021 Market Overview, we openly wondered whether funds with the largest markdowns would have larger (or smaller) rebounds in subsequent quarters. The early evidence suggested there was little relationship between initial markdowns and go-forward performance, which was consistent with the industry's experience in the aftermath of the GFC. We've now updated our initial analysis to include data from Q4 2020:

### Private Equity Q1 2020 vs. Q2-Q4 2020 Performance




Source: Hamilton Lane Data (June 2021)
Bubbles sized by NAV. Y-axis is truncated for visibility. Some individual data ponts may not be visible.

Notice anything (other than a Rorschach-looking smattering of dots)? Maybe a very faint, negative sloping trend? If you drew trend lines for each strategy you would not see a statistically significant relationship. Perhaps looking at summary level clusters will yield more meaningful insights:

### Q2–Q4 Return Quartile Probability Given Q1 2020 Return

| | | Q2–Q4 Quartile | | | |
|---|---|---|---|---|---|
| | | 1st Quartile | 2nd Quartile | 3rd Quartile | 4th Quartile |
| Q1 2020 Quartile | 1st Quartile | 22% | 17% | 24% | 37% |
| | 2nd Quartile | 19% | 24% | 30% | 28% |
| | 3rd Quartile | 27% | 26% | 27% | 20% |
| | 4th Quartile | 33% | 33% | 20% | 15% |

The table above gives the probability that a private equity fund would fall into a specific return quartile based on its Q1 2020 quartile (e.g., the top left corner implies that 22% of funds with a top quartile Q1 2020 return also had a top quartile return in Q2 through Q4).

A few loose “corner” relationships stand out in this view. Funds that generated a fourth quartile return in Q1 2020 (i.e. a larger markdown) tended to have a slightly higher probability of first quartile performance over the subsequent quarters in 2020 and a slightly lower probability of fourth quartile performance. An equally colorful relationship can be found in the top corners of our heat map. In other words, funds that had a top quartile Q1 2020 return were more likely to have a fourth quartile return in subsequent quarters and less likely to have a top (or second) quartile return. In short: There is some evidence that funds that had particularly large (or, in the opposite scenario, small) markdowns in Q1 2020 had better (or worse) experiences in Q2 – Q4 2020.

Astute readers may wonder whether those trends are partially a function of grouping venture capital, growth equity funds, and buyout funds together. A good question – and one that we anticipated. We can confirm that these results are robust at the strategy level, though the relationships are mildly stronger for buyout than they are for venture capital and growth equity.

We’ve admittedly just thrown a lot at you (how many times can we possibly use the word quartile in one paper?), but what does this all mean for LPs? After a period of tightening return dispersion between managers, we are seeing some early evidence that the dispersion between the best managers and average managers is starting to widen, and we expect that widening to continue into 2021. We’re also seeing managers touting what a great 2020 they had (many of their peers had a similarly great year). For LPs, these dynamics place a renewed recognition of the need for robust data and benchmarking tools to evaluate managers, as well as on the importance of manager selection. Particularly during hectic and unpredictable market gyrations, instinct is one thing, but it’s no substitute for being able to rely on data to check your work.



As of June 17, 2021