TO BE

Hamlet

2024 Market Overview

To invest, or not to invest.
That is the question.

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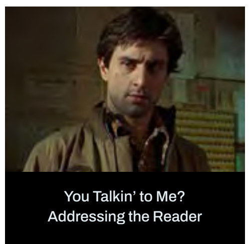
Name the first word that comes to mind when you think about today's private market environment. Drawing a blank? We'll try again. If today's private market environment were a screenplay, which would it be? If you guessed Hamlet (and high fives to anyone out there who did), then you're precisely right!

We appreciate that others of you might be wondering in what alternate universe does "Hamlet" apply to today's marketplace. In an age of artificial intelligence, driverless cars and social media, why on earth is Hamilton Lane talking about some play from centuries past? Wasn't Hamlet a dour Dane who spent his days plagued by indecision while all around him chaos and activity ensued, the purpose and meaning of which were hard to decipher? Hmm, let's see, what if we substituted "Limited Partner" or "General Partner" or "Investor" for "dour Dane?" Are we getting warmer?

We suspect that many of us have spent the last year operating within a mental framework far closer to Hamlet's than we care to admit. Hamlet's tale is that of someone struggling to figure out what to do and, in the retelling, if not the reality of the play, does nothing until it's too late. How many of us this year have worried about how to invest, where to invest and, in the end, didn't do enough investing? How many of us have preferred to contemplate what to do, believing that is an acceptable substitute, given the uncertainty around us, for actually doing something and investing? (Making decisions was so 2022!)

Hamlet's story is about more than that, however; it's also about determining what is real versus what is illusory or fabricated. Prince Hamlet had to question whether the ghost was really his father, whether those around him were giving him trustworthy information or weaving fiction from facts to send him down the wrong path. Those around him, and we as readers of the play, had to determine whether Hamlet was truly mad or merely feigning madness to achieve his goals. Can you not sense some of the similarities in what we're all facing as investors, particularly in the private markets? We are told countless stories of interest rates and inflation, of economic growth and pending recession, of investment returns and the reasons for those returns; all stories that may or may not be correct. We are told what is happening in private markets, and we have to ask ourselves, are those stories factual or are they fiction designed to foster another agenda that has little to do with making good investments?

We have been asked quite often this year how this economic environment compares to that of the Global Financial Crisis (GFC). That request may be more a function of how rare a bear market has been over the last 20 years since the two environments are quite different and it seems curious to compare them.


You Talkin' to Me?
Addressing the Reader

Shakespeare employed a number of narrative devices throughout "Hamlet" and we will borrow two throughout this overview: addressing the audience directly and the soliloquy. Don't worry, we'll signal when we're going there so you're not driven mad trying to figure out if we are or not. (Driven mad…get it?)

Here's one: Ask yourself, as you read on, why people feel as badly about the economic environment today as they do and why they're trying to compare it to the GFC. For the fortunate ones who don't remember the GFC, go watch some media coverage or read some financial news from the period. Today's "economic downturn" has no comparison to that environment. We are in an economic nirvana compared to that era. The fact that we don't believe it or feel it speaks more to the way we absorb information than to anything else. As an investor, that has to set your antenna on high alert. We can argue "this time it's different" and laugh at that argument, but the information backdrop for all of us is different, and far more negative, than ever before. This overview is not the place to debate the reasons why, but it is to highlight that if you aren't factoring that shift into your investment analysis, you're missing a giant piece of the puzzle. It is like looking at a painting of a landscape that has no sky and thinking it is accurate depiction.

We are in an economic nirvana compared to that era. The fact that we don't believe it or feel it speaks more to the way we absorb information than to anything else.

During the GFC, investing felt fairly easy because there were really only two outcomes. It was binary. Either the economic structure was going to collapse entirely, in which case most of your investments were toast, or, it was going to be saved, in which case your investments were going to be fine. These days, we all wish for that kind of clarity. We can, today, create multiple outcomes, all with a great deal of credibility: high inflation and higher rates, deflation and near-zero rates; normal economic growth, recession; decreasing global conflicts, increased and catastrophic global confrontations. The list goes on. That is a tough backdrop for making investment decisions.

Oh, Prince Hamlet, would that you could make a choice…

Not to worry. Hamilton Lane is here to help. We set out in this year's market overview to take stock of what's going on in the investment universe and attempt to identify what is fact and what is only masquerading as fact. Spoiler alert, there's a good deal of the latter. We'll share a ton of information that you won't find anywhere else, and we'll put it out there for you to analyze and, in the end, for you to make the choices. But hear us clearly on this: Make those choices. Remember, doing nothing is actually doing something. It's a bit passive aggressive, and while we can recommend a Dr. Freud in Vienna who could help, we're confident he'd back us up in saying that making choices is important. We like to think that if we were around in Prince Hamlet's day, we could have written him a market overview to help him understand what was happening around him. He would have deposed the king, reconciled with mom, married Ophelia, had a bunch of little Hamlets and Hamlettas, and put all his savings into private markets instead of the military and we would all be speaking Danish in the global United Kingdom of Denmark.

Our aspirations have always been modest, haven't they?

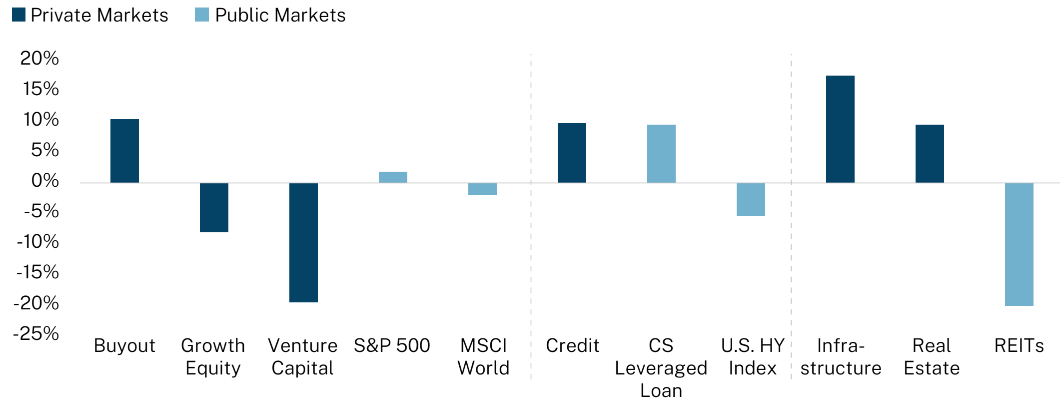
But enough frivolity, follow us, my princes and princesses, and let's find answers to all our investment questions, because something is decidedly NOT rotten in the state of the private markets.

Let's begin by looking at a few ways to assess performance.

Performance

Chart 1.1: Private & Public Market Returns

Q4 2021 - Q3 2023



Source: Hamilton Lane Data, Bloomberg (January 2024)

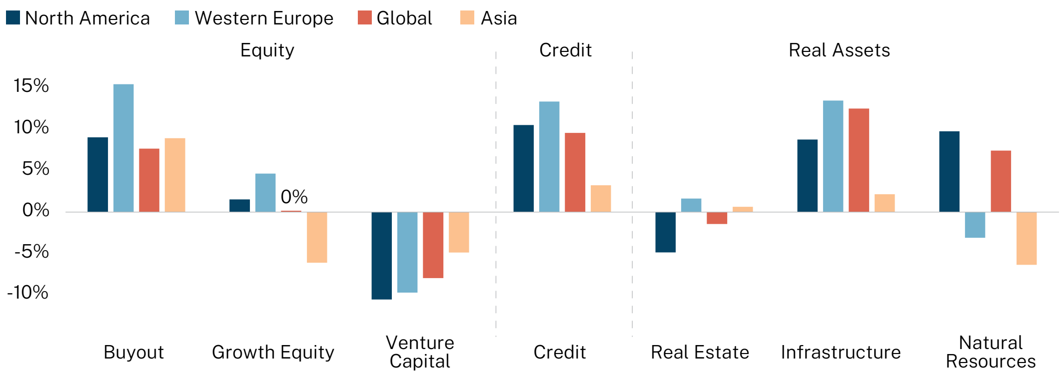
Chart 1.1 looks at performance from the end of Q4 2021 to the end of Q3 2023. Why that seemingly random time period? Because it spans the point at which the public markets peaked to the most recent data at the time we wrote this overview. Remember last year, how everyone screamed that private markets, particularly private equity, had bogus numbers and couldn't continue to outperform the public markets?

(You want to feel old? That song was released 24 years ago...)

Credit, infrastructure and real estate continue to outperform their public comparables. Buyout does too. *By a lot*. Apologies to anyone expecting something different, but reality can sometimes bite. As we pointed out last year, venture and growth continue to struggle. That's a trend we suspect will continue, but that's a tale for another part of this overview.

Let's look at the numbers somewhat differently. (Get used to hearing that if you haven't read these overviews before. We are big believers in looking at the same topic and slicing the data in a number of different ways employing different methodologies. You know the cliché: Numbers can be made to tell any story. But give me enough stories with different numbers and I should be able to tell a more accurate story.)

Chart 1.2: Pooled One-Year IRR by Asset Class and Geography



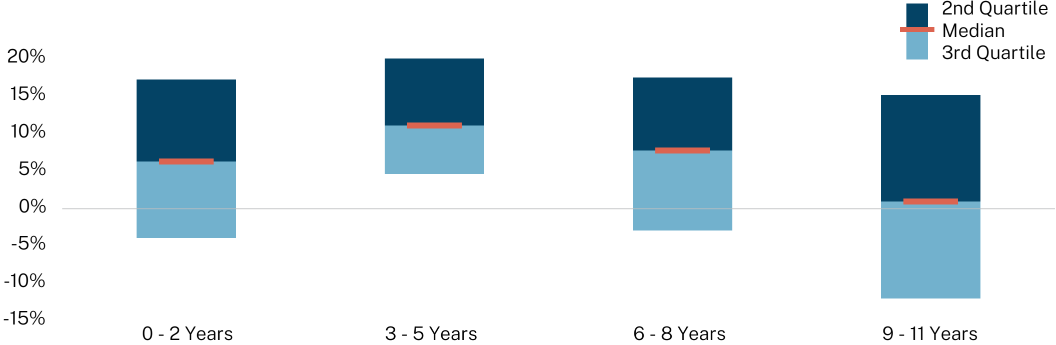
Source: Hamilton Lane Data (January 2024)

Ok, lots of bars in Chart 1.2. What we're showing here is pooled IRR on a one-year, point-to-point time frame, across 10 vintage years. This gives perspective both on performance across various sub-classes in private markets and how geography impacted that performance. It is interesting to note that infrastructure and venture capital are the most consistent performers across geographies (albeit in opposing directions), while growth equity, real estate and natural resources are the most inconsistent. Credit and buyout have been good performers, but your geographic allocation mattered a lot. Europe rocked, particularly for USD-denominated investors!

Long-time readers, prepare your ears (err, eyes).

We've harped on the importance of portfolio construction for what feels like forever, and we are going to do it once more. It matters more than almost anyone in the private markets universe is willing to acknowledge or practice. Take a look at this next chart.

Chart 1.3: Dispersion of One-Year Buyout IRRs by Fund Age



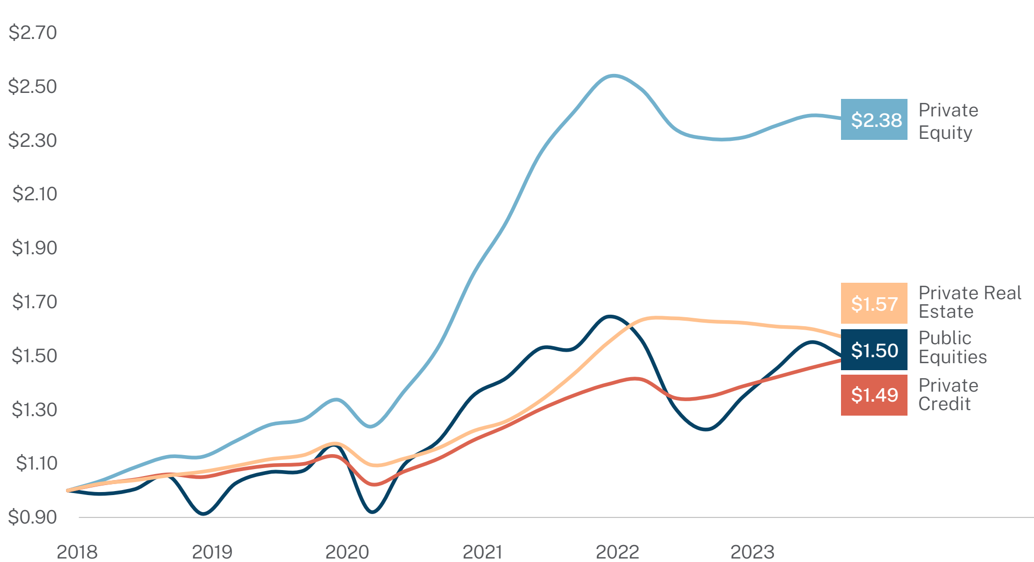
Source: Hamilton Lane Data (January 2024)

We're again looking at one-year, point-to-point performance, but this time we are looking at returns by the age of the fund. Think it's all the same? We always assume that younger funds don't perform as well because of the J-curve. You wonder if that is something that is changing in the private world (that is a more macro subject that deserves far more coverage than just a teaser left here, but that is all it gets for now). The worst-performing funds over this one-year period, and with the widest dispersion of return, are the oldest funds. The performance sweet spot is the three-to-five-year-old funds, those just outside their investment period. Interestingly, they combined better performance with lower dispersion.

Still don't think this matters? Think you are immune from these considerations because you invest evenly every year? Well, consider this: You don't invest evenly every year. Sorry, it had to be said. Ok, how about your favorite secondary fund or purchases—what vintage are they buying? How's that working? What about funds you have sold? Old or new? Borrowed or blue? (We get carried away and throw in those lines just to see if you're paying attention).

Let's go back to overall asset performance and look at the performance of various asset classes over the last five years.

Chart 1.4: Growth of $1

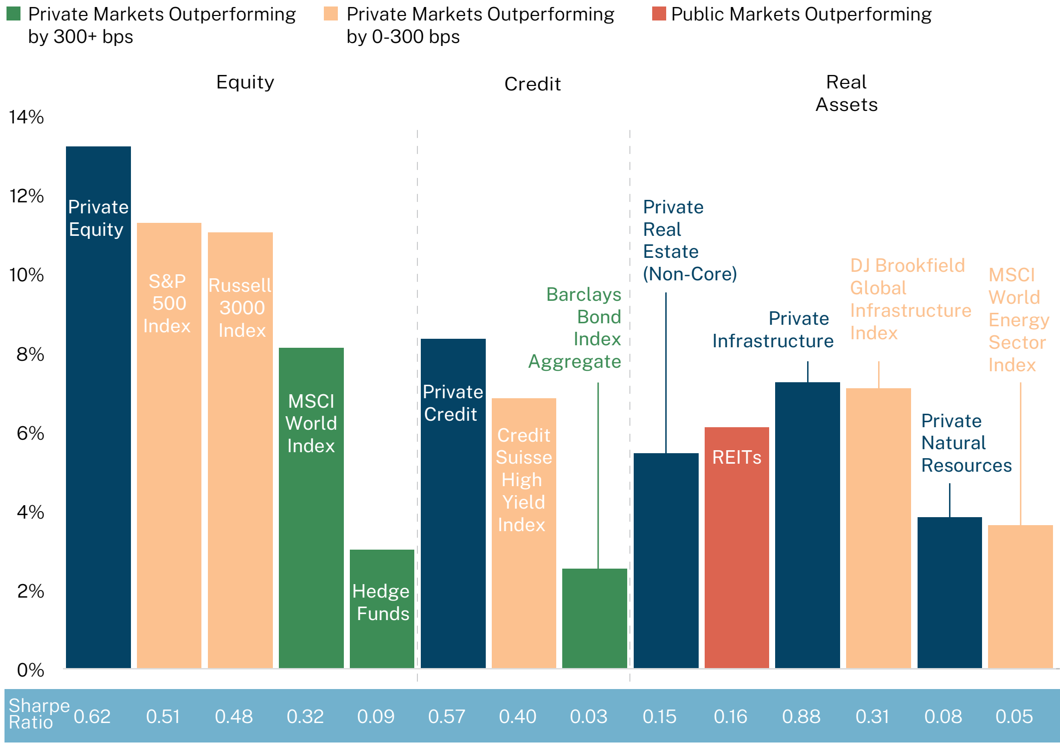


Source: Hamilton Lane Data via Cobalt, Bloomberg (January 2024)

What more can you say about this? One dollar (it's the same if you configure this in euros or yen or pounds or the currency of your choice) in private equity is worth a whole lot more than one dollar in public equities. We say it every year, and some doubt us every year. Over that period, you got higher upside and lower downside in private versus public. Equally amazing is that you got almost the same return from private credit and real estate as you did from public equity. Who knew? Let's go back even farther.

Chart 1.5: 15-Year Asset Class Performance

Annualized Time-Weighted Return as of Q3 2023

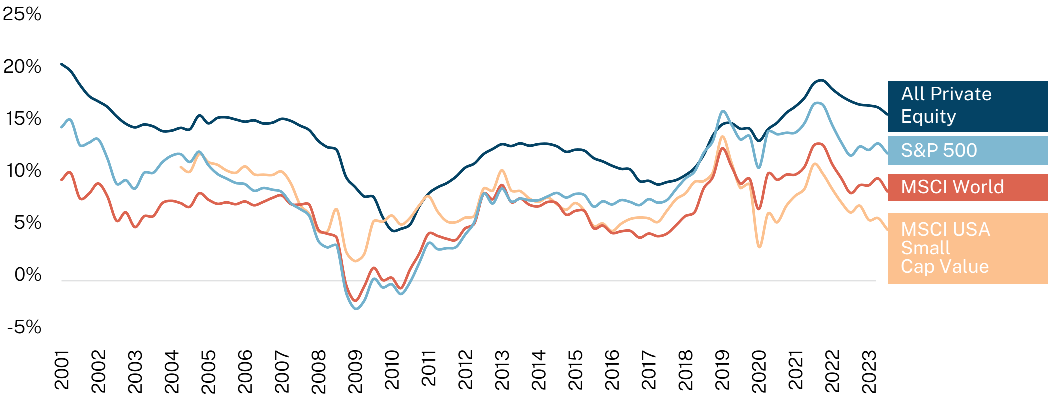


Source: Hamilton Lane Data via Cobalt, Bloomberg (January 2024)

We show Chart 1.5 every year, though admittedly we're not sure why, since it shows pretty much the same thing every year. Maybe because, if we didn't, those private market haters would leap through this page and say, "Hey, where's the 15-year chart? I bet Hamilton Lane isn't showing it because it doesn't show outperformance."

Sigh. It does. Again. Even against the U.S. indices, the strongest performers in the world over the last 15 years, private equity outperformed. There's only one red spot on this chart: REITs outperformed private real estate. Shout out to anyone out there who has a 100% REIT portfolio! (Kidding aside, we'd note that the entire outperformance is due to the lousy performance of the GFC-era funds in this comparison. It's hard to believe that history will repeat.) As we leave this chart, we will not take our traditional, annual cheap shot at hedge funds. Only because we couldn't bring ourselves to put the words "cheap" and "hedge funds" in the same sentence. (Or could we...)

Chart 1.6: All Private Equity 10-Year Rolling TWRs



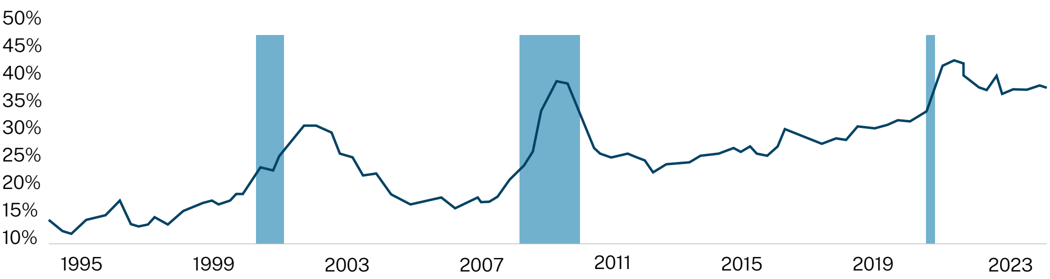
Source: Hamilton Lane Data, Bloomberg (January 2024)

Chart 1.6 remains one of the more important in this overview. Here we're measuring rolling, 10-year performance numbers of private equity versus various public indices. And we're doing so using time-weighted returns to make it more apples-to-apples to how public index returns are calculated. (Before you ask, no, using IRR and PMEs won't change the results much…) This chart matters because investors typically think of private equity exposure against a 10-year investment horizon. Look at these squiggles. We are asked constantly whether now is the time to invest in private equity. The answer, for the last almost 25 years is, yes, now is the time. There are very few 10-year periods where private equity didn't outperform, and did so handily. Isn't that what everyone wants from their investments?

Alas, poor private markets, prepare thyself for a soliloquy… The stage is empty, save for Hamilton Lane and, in the background, Chumbawamba's "Tubthumping" is playing…

We wonder, as we go over these charts, why there is so much skepticism about private markets, particularly private equity and buyouts. We saw a major publication recently refer to private equity's underperformance in certain 10-year periods. We look at Chart 1.6 and think, there is one period where that is true, ending around 2019 against the S&P 500, and one period ending around 2010 against the MSCI Small Cap Value Index. The publication's author implied that underperformance was a common occurrence. Seriously? What are we to make of that bias and creative juggling of data? We can't bring our chart out to counter that argument; most people would fall asleep before we got to the second sentence of the explanation. And, as we contemplate this in the quiet of our Creative Services Laboratory (it's not actually quiet and, in fact, we have our dogs here with us), there's another generally unasked question about what that performance is actually measured against. When we say, "private equity outperformed against a public market index," there is an assumption that the portfolios have some similarities. Do they?

Chart 1.7: **Percentage of Russell 2000 Companies with Negative Earnings**

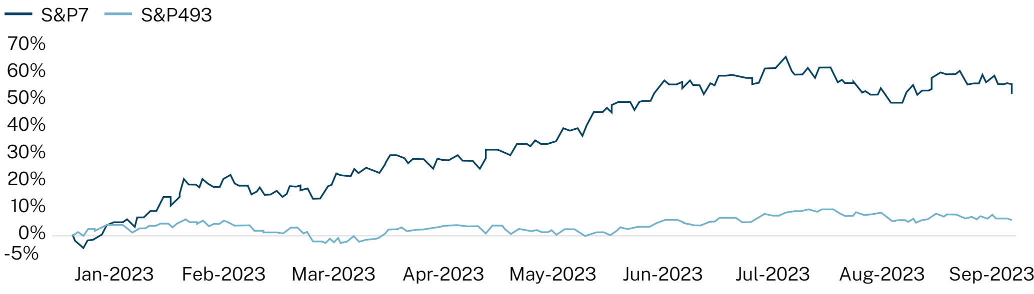


Source: Apollo Chief Economist (December 2023)

40% percent of companies in the Russell 2000 have negative earnings. (That's "lost money last year" for those who speak like the rest of us.) What if we were told that 40% of companies in our private equity portfolios lost money last year? Imagine the cry of "this is false accounting… these companies are worthless!" They apparently aren't worthless in the public markets and, in fact, are being used as comparables against a set of financially stronger companies. There's another set of numbers that tells us that time is not the only thing out of joint (go ahead, find all the "Hamlet" references in this overview).

Chart 1.8: **S&P Constituent Cumulative Performance**

Percent Change Since January 1, 2023



Source: Bloomberg, Apollo Chief Economist (October 2023)

We are borrowing (stealing, despite the admonishment to be neither a borrower nor a lender) this chart from Torsten Slok at Apollo. (We must remind everyone when we leave this soliloquy that if they do not read his daily newsletter, they should.) It tells us that seven companies in the S&P 500 have driven all the performance of that index. That is vastly different from the diversification you see in private equity portfolios. What would investors say if we told them that about 1% of their private equity portfolio drives all of their results? They would be screaming about the outsized risk and avoiding the asset class like the plague. But, hey, we are fine with a lack of diversification. If it gets results, go for it. But wait, there's more. What, pray tell, is the average P/E ratio of that S&P 7 set of companies? At a recent reading, it was around 45. Forty-five! What if we came to our investors and said, "Your private equity portfolio is entirely driven by 1% of the companies in there and their average P/E is 45?"

Imagine what the major publication would have to say about investors going into those investments…

The following two charts appear in all our market overviews and we've contended they are the most important in the book. (At least until another chart catches our eye, that is.)

Chart 1.9: Buyout IRR vs. PME

By Vintage Year

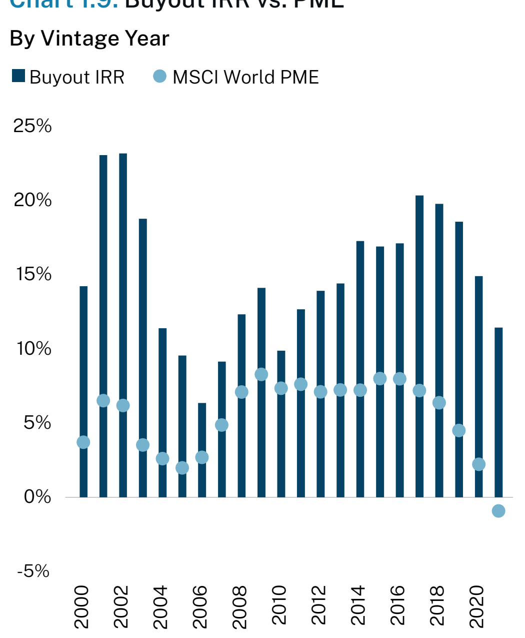
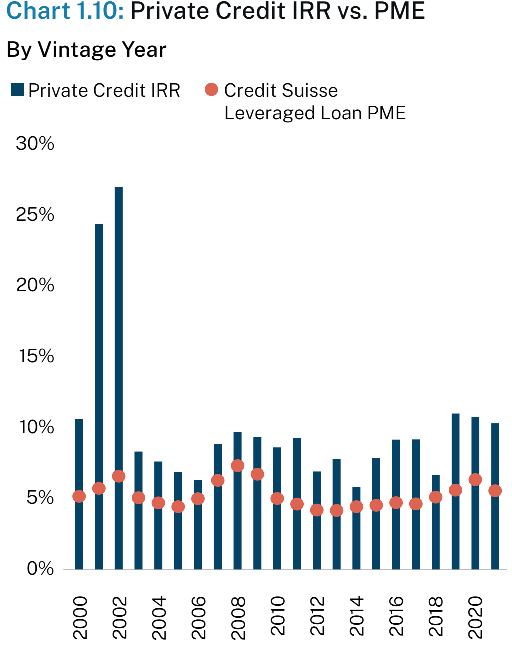


Chart 1.10: Private Credit IRR vs. PME

By Vintage Year



Source: Hamilton Lane Data via Cobalt, Bloomberg (January 2024)

The data tells a simple story: Pooled buyout returns (not only top quartile, not a curated portfolio), on a PME basis (same dollars into and out of the public index) have outperformed public market returns *in every one of the last 22 vintage years!* And how did credit stack up? Why, credit also outperformed leveraged loans in *each one of the last 22 vintages.* (If only we could insert an audio clip here of angels singing Hallelujah…)

That pretty much says it all and, again, makes you wonder why there is so much skepticism about private markets. Sure, things might turn out differently going forward. But ask yourself, "*Why will it be different? Didn't you, oh Hamlet, fret and moan over pretty much the entirety of these last 22 years about whether that outperformance could continue? The markets were up, you worried; the markets were down, you worried; the markets were flat, you worried; the markets were closed on weekends and holidays, you worried. As you worried, private markets outperformed, year in and year out.*"

Brevity is the soul of wit, and private markets are the soul of sound investments.

Let's be fair and present real estate and infrastructure on the same terms.

Chart 1.11: Real Estate IRR vs. PME

By Vintage Year

Real Estate IRR | FTSE/Nareit Equity Index PME

Chart 1.12: Infrastructure IRR vs. PME

By Vintage Year

Infrastructure IRR | DJ Brookfield Global Infrastructure PME

Source: Hamilton Lane Data via Cobalt, Bloomberg (January 2024)

It's not a 22-year history of outperformance, but rather more like 10 to 15 years. These real asset categories suffered during the GFC, and yet they have thrived since. Some may argue that's a function of lower interest rates over the last ten years, but that's not what's going on here. The real reasons are different for each. As mentioned earlier, real estate's pre-GFC funds were, stated in an investment vernacular, crushed. Just crushed. There's no getting around that period. Infrastructure has a different explanation, and it's that the market has changed substantially since the 2002 to 2010 time frame. The infrastructure funds of that era are like the land of misfit toys: emerging market funds and energy funds, in particular, that bear little to no resemblance to the infrastructure funds and investments of today.

Chart 1.13 has appeared in every overview and makes its way into numerous presentations throughout the year.

Real estate's pre-GFC funds were, stated in an investment vernacular, crushed. Just crushed.

Chart 1.13: Periodic Table of Returns

Pooled IRR by Vintage Year

Vintage Year	Above All PM (top to bottom)	All PM	Below All PM (top to bottom)
2003	EU Buyout 21.4%; U.S. SMID 15.1%	All PM 12.2%	Mezzanine 10.0%; Real Estate 8.9%; Distressed Debt 7.2%; Late-Stage VC 3.4%; Seed/Early VC 0.5%
2004	Natural Resources 26.8%; Real Estate 15.5%; EU Buyout 14.8%; ROW 12.2%	All PM 11.6%	U.S. SMID 10.8%; U.S. Large/Mega 10.6%; Distressed Debt 8.6%; Multi-Stage VC 8.0%; Seed/Early VC 7.9%; Mezzanine 4.1%
2005	Seed/Early VC 14.6%; Natural Resources 12.8%; Growth Equity 12.0%; EU Buyout 10.7%; U.S. Large/Mega 10.0%; U.S. SMID 9.7%; Infrastructure 9.4%; Distressed Debt 8.2%	All PM 7.6%	Mezzanine 7.2%; Multi-Stage VC 6.6%; ROW 5.9%; Real Estate -0.4%
2006	Late-Stage VC 14.6%; Distressed Debt 8.9%; Growth Equity 8.3%; U.S. SMID 7.8%; U.S. Large/Mega 7.1%; Multi-Stage VC 6.9%; Mezzanine 6.7%	All PM 4.9%	EU Buyout 4.5%; Infrastructure 4.0%; ROW 3.5%; Seed/Early VC 3.3%; Real Estate -0.1%; Natural Resources -5.2%
2007	Seed/Early VC 12.1%; U.S. SMID 12.0%; Multi-Stage VC 11.4%; Growth Equity 10.7%; U.S. Large/Mega 10.3%; Distressed Debt 9.3%; Mezzanine 8.8%	All PM 7.4%	EU Buyout 5.9%; ROW 5.6%; Infrastructure 5.2%; Natural Resources 4.0%; Real Estate 1.5%
2008	Growth Equity 21.5%; Seed/Early VC 17.4%; U.S. SMID 13.8%; U.S. Large/Mega 13.7%; Late-Stage VC 12.2%; EU Buyout 11.9%; Multi-Stage VC 11.4%; Mezzanine 10.8%	All PM 10.5%	Distressed Debt 10.4%; Infrastructure 7.5%; ROW 7.1%; Real Estate 7.0%; Natural Resources -2.9%
2009	U.S. SMID 20.0%; Multi-Stage VC 17.1%	All PM 11.4%	EU Buyout 11.2%; Mezzanine 10.2%; Distressed Debt 9.9%; Real Estate 9.8%; Seed/Early VC 9.2%; Infrastructure 7.7%; ROW 5.9%; Natural Resources -5.9%
2010	Seed/Early VC 41.6%; Stage VC 16.8%; U.S. SMID 13.6%; Real Estate 13.1%	All PM 11.9%	EU Buyout 11.7%; Mezzanine 9.3%; Distressed Debt 8.0%; ROW 5.8%; Natural Resources -0.4%
2011	Seed/Early VC 29.7%; Multi-Stage VC 20.5%; Growth Equity 19.6%; U.S. SMID 17.5%; Real Estate 17.2%; U.S. Large/Mega 15.5%; EU Buyout 14.0%	All PM 13.2%	Distressed Debt 9.4%; Mezzanine 8.7%; ROW 4.9%; Infrastructure 3.8%; Natural Resources 1.3%
2012	Seed/Early VC 27.8%; Multi-Stage VC 20.2%; Late-Stage VC 18.6%; U.S. Large/Mega 18.5%; Growth Equity 15.0%; U.S. SMID 14.6%; Infrastructure 14.4%	All PM 12.0%	EU Buyout 11.7%; ROW 9.1%; Mezzanine 8.8%; Real Estate 8.5%; Distressed Debt 6.5%; Natural Resources 1.2%
2013	Multi-Stage VC 20.9%; Seed/Early VC 19.1%; Growth Equity 19.1%; U.S. SMID 16.2%; U.S. Large/Mega 16.0%; Mezzanine 13.3%; EU Buyout 13.2%	All PM 11.5%	Real Estate 10.6%; Infrastructure 10.0%; ROW 8.7%; Distressed Debt 7.2%; Natural Resources 1.1%
2014	Late-Stage VC 36.7%; Seed/Early VC 21.3%; U.S. Large/Mega 20.2%; Multi-Stage VC 19.5%; Growth Equity 19.5%; EU Buyout 19.2%; U.S. SMID 15.3%	All PM 13.8%	ROW 13.4%; Infrastructure 12.1%; Real Estate 8.6%; Mezzanine 5.7%; Distressed Debt 5.2%; Natural Resources 4.4%
2015	Seed/Early VC 23.7%; Growth Equity 22.8%; U.S. SMID 19.5%; Late-Stage VC 18.6%; U.S. Large/Mega 17.8%; EU Buyout 15.6%	All PM 14.0%	ROW 13.3%; Multi-Stage VC 12.5%; Real Estate 12.2%; Natural Resources 10.8%; Mezzanine 9.2%; Distressed Debt 7.9%; Infrastructure 6.8%
2016	Seed/Early VC 31.6%; Growth Equity 26.4%; U.S. SMID 20.5%; EU Buyout 16.5%; U.S. Large/Mega 15.4%	All PM 15.3%	Multi-Stage VC 14.7%; ROW 14.4%; Real Estate 11.1%; Infrastructure 10.6%; Distressed Debt 9.9%; Mezzanine 9.1%; Natural Resources 7.0%
2017	Growth Equity 24.4%; U.S. SMID 22.3%; U.S. Large/Mega 21.8%; Seed/Early VC 20.2%; Multi-Stage VC 17.8%; EU Buyout 17.6%	All PM 16.6%	Natural Resources 14.5%; ROW 12.4%; Infrastructure 11.4%; Real Estate 11.1%; Mezzanine 10.3%; Distressed Debt 8.2%
2018	Seed/Early VC 25.8%; EU Buyout 22.7%; Growth Equity 21.9%; Multi-Stage VC 21.0%; U.S. Large/Mega 20.9%; U.S. SMID 19.7%; Late-Stage VC 19.7%; Natural Resources 17.9%	All PM 15.9%	ROW 13.9%; Real Estate 11.1%; Infrastructure 10.1%; Mezzanine 9.8%; Distressed Debt 5.2%
2019	Late-Stage VC 27.1%; Growth Equity 22.3%; U.S. SMID 20.5%; Seed/Early VC 20.3%; U.S. Large/Mega 19.7%; Natural Resources 15.9%	All PM 15.7%	EU Buyout 14.5%; Real Estate 14.2%; Mezzanine 11.9%; ROW 11.7%; Multi-Stage VC 11.6%; Distressed Debt 10.6%; Infrastructure 10.5%
2020	Natural Resources 32.4%; U.S. SMID 17.5%; Seed/Early VC 17.5%; U.S. Large/Mega 14.9%; Growth Equity 13.6%	All PM 13.0%	Distressed Debt 12.0%; ROW 12.0%; EU Buyout 11.7%; Mezzanine 10.5%; Real Estate 9.6%; Late-Stage VC 9.2%; Multi-Stage VC 8.9%; Infrastructure 6.8%

☐ Negative returning strategy

Source: Hamilton Lane Data (January 2024)

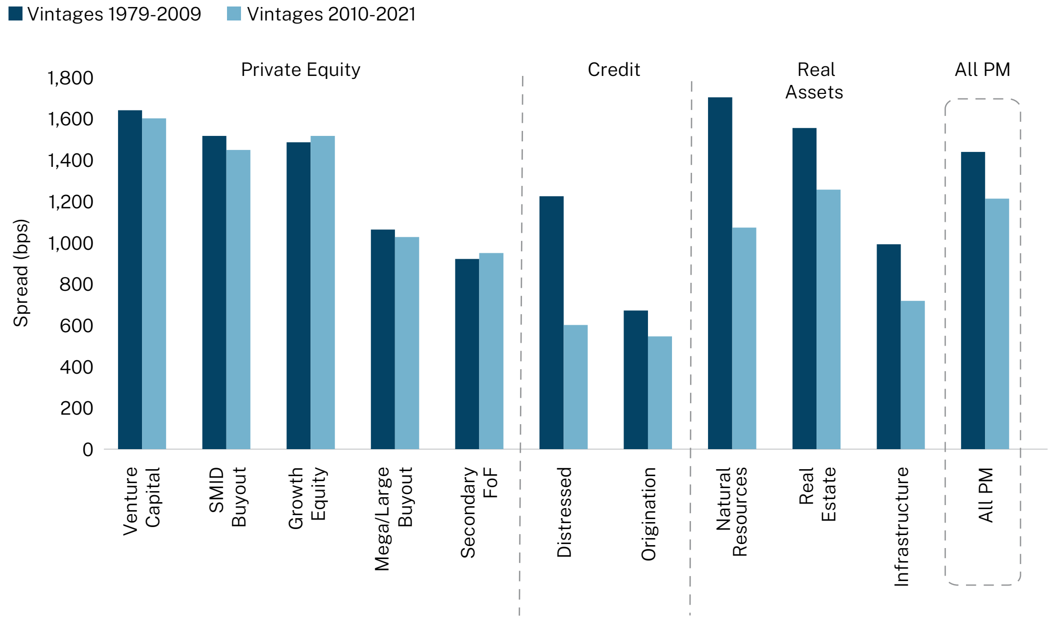
It tells a story that probably warrants constant retelling, because it goes to the heart of why portfolio construction matters:

- Most strategies are, on average, where you'd expect them to be in the rankings. Equity on top, credit and real assets lower down. There are some years that run counter to that trend, but it is really hard to pick those years ahead of time. Developing a plan and sticking to it is the best way for most investors. Timing the exact movements is foolish.
- Don't lose sight of how impressive "All PM" returns are every year. You are doing pretty well being average. Really well.
- Also, don't lose sight of how hard it is to lose money in fund investments. There's a view that private investors lose money all the time. They don't. (Here's one of those fact vs. fiction debates we hinted at in the intro. Fact 1; Fiction 0.)
- Think carefully about your risk/return targets. Many investors love to trash standard buyout, particularly the larger funds. We don't like to say this in polite company, but there are even years when larger funds have bested their smaller peers. (Go ahead and take a moment to compose yourself after that shocker.) Buyouts never show up as top performers over the last 15 years. But, guess what? They don't show up as bottom performers either. They are steady and perform consistently very well. Again, you could do far worse as an investor than someone who simply puts all their money in boring buyout and goes into Rip Van Winkle mode for the next decade.

Hey, Hamilton Lane, how about sprinkling in some new charts and not just updated re-treads? Here's one you'll love.

Chart 1.14: **Dispersion of Returns by Strategy**

By Vintage Year Groupings; Ordered by Long-Term Spread of Returns



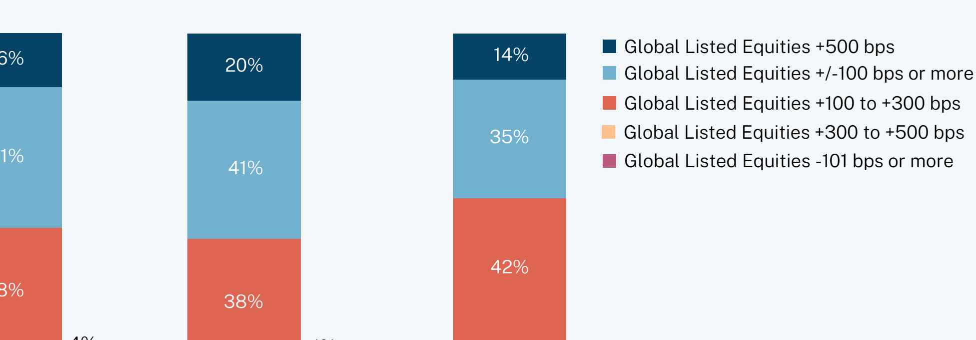
Source: Hamilton Lane Data via Cobalt (January 2024)

Chart 1.14 tells you two things, one of which you already know: There are significant dispersion differences among the various private investment sub-categories. Investors can become enamored with a portfolio stuffed with venture, growth and small buyout. Sure, everyone should consider some exposure because the returns can be so much higher than other categories. But so is the risk. We are always amazed, by the way, at how secondary funds, that so many use as J-curve mitigators, are actually risk/return enhancers.

Now for the second thing. We constantly hear the refrain that, as private markets grow, the dispersion will decrease as the markets become more efficient. What we show in Chart 1.14 is the difference in that dispersion from the years 1979 to 2009 compared to the last 11 years. If that efficient market theory were true, we should expect the dark blue bar to be far higher than the light blue bar. So, are we operating with facts or fabricated theories? Dispersion of private equity returns has come down by so small an amount that it is hardly worth considering. Only distressed credit and natural resources saw any substantial decrease. Real estate experienced some spread compression, but the larger spread in earlier years was driven primarily by GFC-era funds. Surprised? There are probably numerous theories that the theorists will propose because that's what theoreticians do, but for those of us who invest, the data is clear: There is little increasing efficiency in the majority of the private markets.

We like asking general partners every year what they think is going to happen in the future. (And, shockingly, they like sharing their opinions. It's a win-win!) This year's take represents the responses from 116 GPs around the globe.

Chart 1.15: GP Survey – Net returns for all private markets for the following three vintages will be...



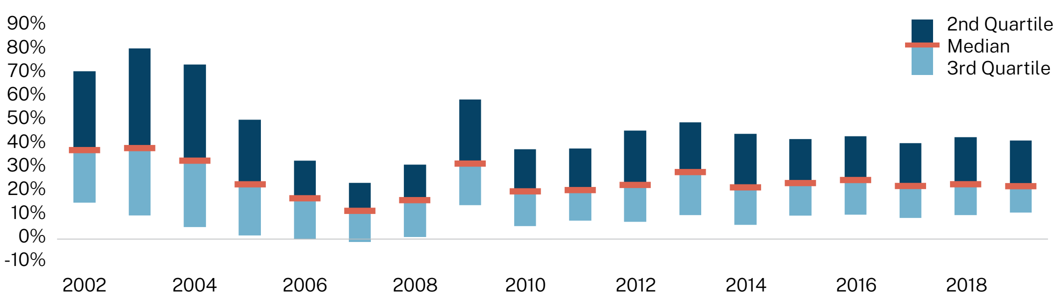
Source: Hamilton Lane General Partner Survey 2023 - 2024 (December 2023)

They are an optimistic lot by nature (we try to keep the number of credit managers – a typically morose lot – to a manageable level), but you can see that they are more pessimistic this year than they were in prior years. GPs still believe private markets returns will handily outpace the public markets, but the margin is less than we have seen previously.

Let's turn to gross deal returns. This is not fund-level returns, but what the underlying deals themselves are doing.

Chart 1.16: **Gross Buyout Deal IRR Quartiles**

By Deal Year



Source: Hamilton Lane Data (January 2024)

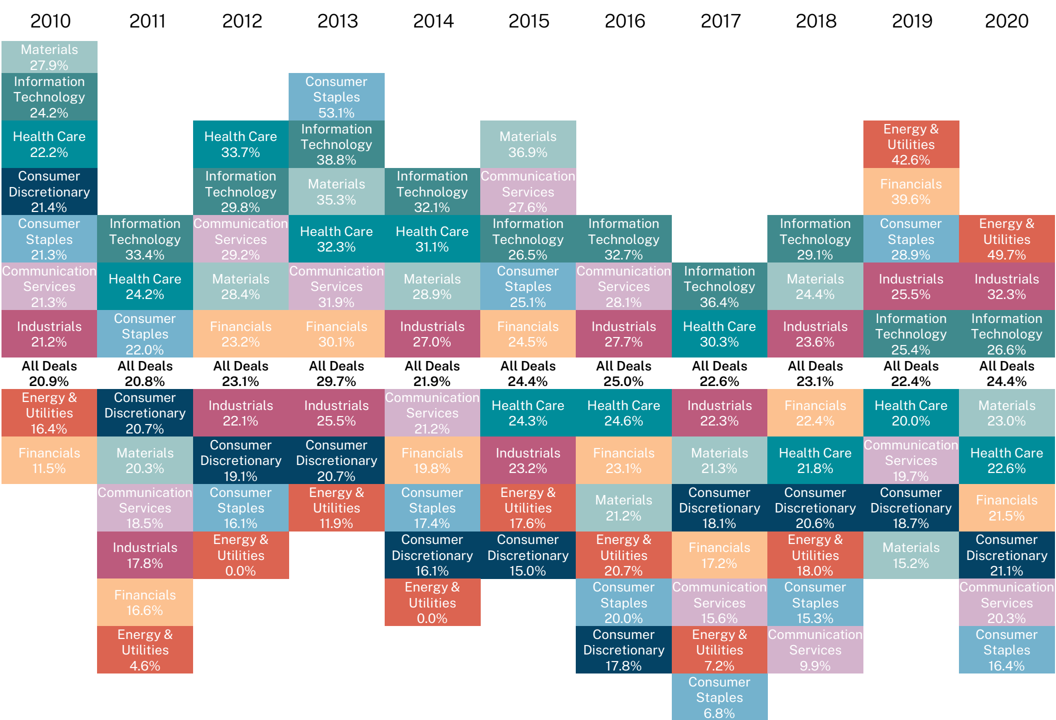
We make this statement every year, but it bears repeating every year: My God, it is good to be a general partner. This is why, as we'll show later, everyone still wants to be one, irrespective of the fundraising environment. It is truly a tails I win, heads you lose proposition when you see these numbers. We can argue, as many do, that this reflects the fact that GPs are simply better investors, and that may be true. But their handsome rewards for that investment acumen, as every limited partner will tell you, are what make the LP community crazy. Fees and carry on these figures are enormous and contribute to the industry being generally regarded with so much skepticism and suspicion by the investing community, politicians and the media. Will the fees change? We have been dubious that would happen in the absence of a massive downturn in the industry, particularly one where returns are chronically underperforming public markets. We don't see that environment coming any

My God, it is good to be a general partner. It is truly a tails I win, heads you lose proposition.

time soon, so we don't see a reason for fees to decline much.

Chart 1.17: Periodic Table of Gross Returns

Sector Median Gross IRR by Deal Year



Source: Hamilton Lane Data (January 2024)

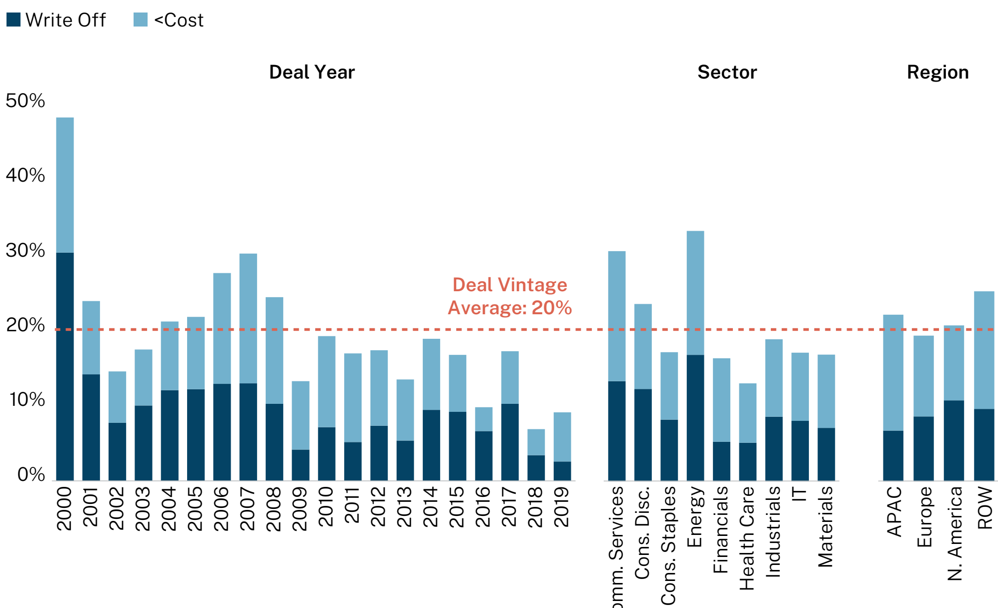
Certain industries have been at both the top and bottom of the chart for the last decade. Why? We're not sure we have an answer on that one. What remains interesting is how difficult it is to lose money consistently – or even at all if we look across this 2010-2020 timeframe. Sure, energy investments may not have made any money in 2012 or 2014, but they didn't lose money either. The other interesting number is that "All Deals" return. Want to know another difference between appearance and reality in the investment world? Consider this phrase that we have all heard over and over for the last decade (actually, for the last 30 years): Private equity returns are coming down.

What a piece of work is accepted wisdom.

This is not to say that you can't lose money on individual deals. You certainly can.

Chart 1.18: Loss Ratio of Realized Buyout Deals

% of Deal Count



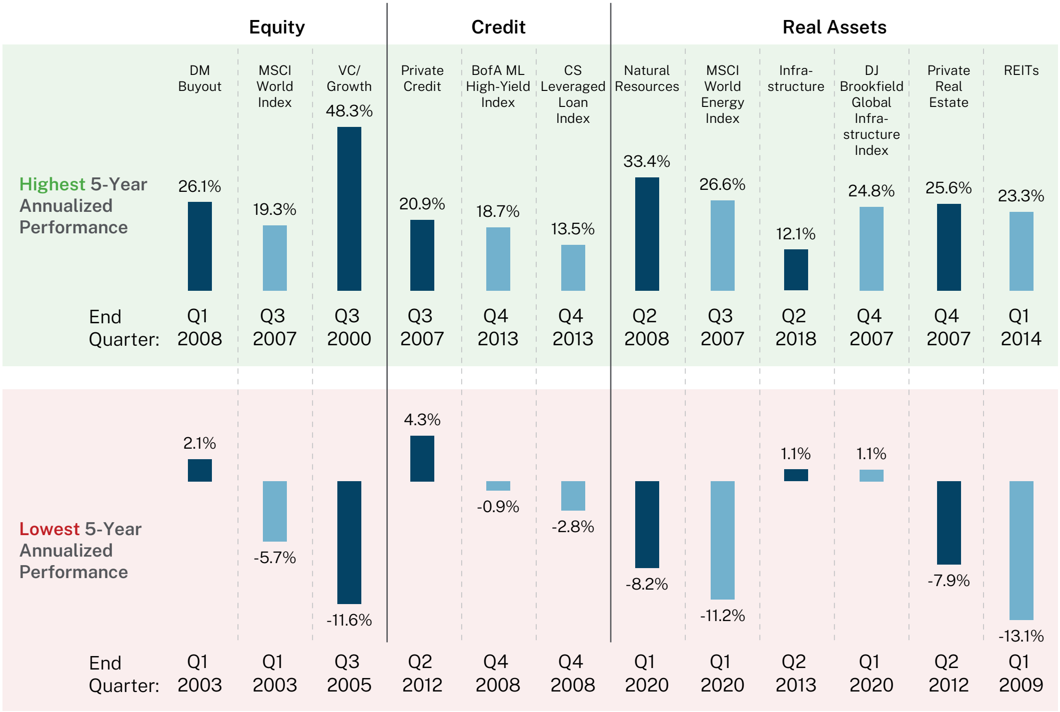
Source: Hamilton Lane Data (January 2024)

In fact, you should expect to lose money on roughly 20% of your underlying transactions. The asset class has been running well below that recently, but don't expect that trend to continue. (Yes, we will give bad news when we see it.) It is why, after all, you diversify your portfolios. (Umm, co-investors please take note…) We're reminded of a truism shared with us once by a highly skilled investor: If you are not losing some money on some of your investments, you are probably not taking enough risk.

We think that is one of the more important pieces of investment advice we have ever heard. For anyone contemplating all the reasons why you should remain frozen and not invest given the uncertainty, remember that you have to risk something to gain something. It's how things work in all areas of life, including investments.

You knew we'd get to risk, right? Here's the most important chart (we reserve the right to say that more than once!) in the overview.

Chart 1.19: Highest and Lowest 5-Year Annualized Performance



Infrastructure from 2006-2023, Natural Resources from 1998-2023
Source: Hamilton Lane Data via Cobalt, Bloomberg (January 2024)

Let your eye wander down to the bottom set of figures. Cowabunga! The conventional wisdom is that private markets are risky, and you can lose so much money. (Like, so much.) What's the reality? Over the worst five-year period in developed markets buyout, private credit and infrastructure, *you didn't lose any money*. Let us say that again. *You. Didn't. Lose. Money.* That is not true of any other investment area. Aha, you say, well I sure must have given up some upside to get that amazing downside protection. Nope. Better upside. Better downside.

Why Past Performance Cannot Continue

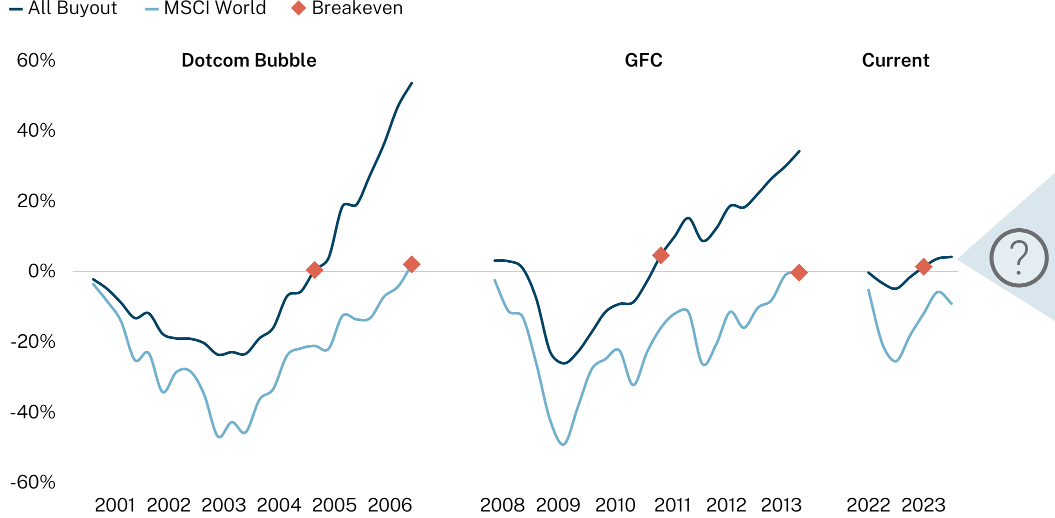
Amid the never-ending chatter about private markets, there is one constant refrain that keeps so many investors paralyzed by indecision: "Yes, but that outperformance can't continue." Normally, no reason or explanation is offered; it is instead simply an accepted fact, a façade over any underlying reality. It has been said for so many years that, well, it must be true. Saying it doth make it so. (Eh, sort of a weak attempt at Hamlet-speak, but allow us poetic license.) If you probe into today's environment, you get a few reasons why this outperformance won't continue.

Valuations Are Inaccurate

We can't tell if this is a real one today or just a bad hangover from 2022's party-crashing histrionics. Throughout 2022 and early 2023, it was broadly decided that private equity couldn't be flat let alone up when the public markets were down 20%. It had to be a valuation gimmick that would correct at some point in 2023. That didn't happen, especially since the public markets decided to move up, but some people hold steadfast to their belief that the day of valuation reckoning is near. Let's consider some facts around this developing mythology, shall we?

Chart 2.1: Cumulative Returns During a Crisis

Buyout vs. Global Equities Cumulative Returns



Source: Hamilton Lane Data, Bloomberg (January 2024)

So many people acted as though private equity's outperformance as public markets got crushed was unprecedented. It wasn't. (Just a general life note: The word "unprecedented" gets thrown around a lot lately. Our rule is simple: When we hear that word uttered, we know what's being described has invariably happened before and probably pretty often. But whoever has used that word doesn't have the perspective to know that. It says more about the speaker than the event.) Private equity handily outperformed – by roughly the same 2,000 basis points – in both prior severe public market downturns. Don't you hate it when facts get in the way? What is noteworthy is that, in both prior cycles, private equity returns didn't flatten or go down to make up for the "valuation BS" that was going on during the downturn. No, those valuations and returns kept trending upward along with the public markets. Logic suggests that, were those valuations inflated, that would have been reflected in future time periods. This cycle's history has yet to be written, but it seems different thus far in that the downturn is shallower and the upturn faster than either the dotcom or GFC era. History suggests that, if the downturn has ended, private equity returns will rise farther and faster than public markets over the recovery cycle.

That deals with the answer of "what has happened," but doesn't address the "why." There are a few reasons why we believe both the valuations are realistic and there is no future downturn based on inflated valuations today.

Chart 2.2: Median Operational Performance

North America Buyout
S&P 500
20%
15%
10%
5%
0%
-5%
Revenue
EBITDA
Enterprise Value
2022
2023 YTD
2022
2023 YTD
2022
2023 YTD

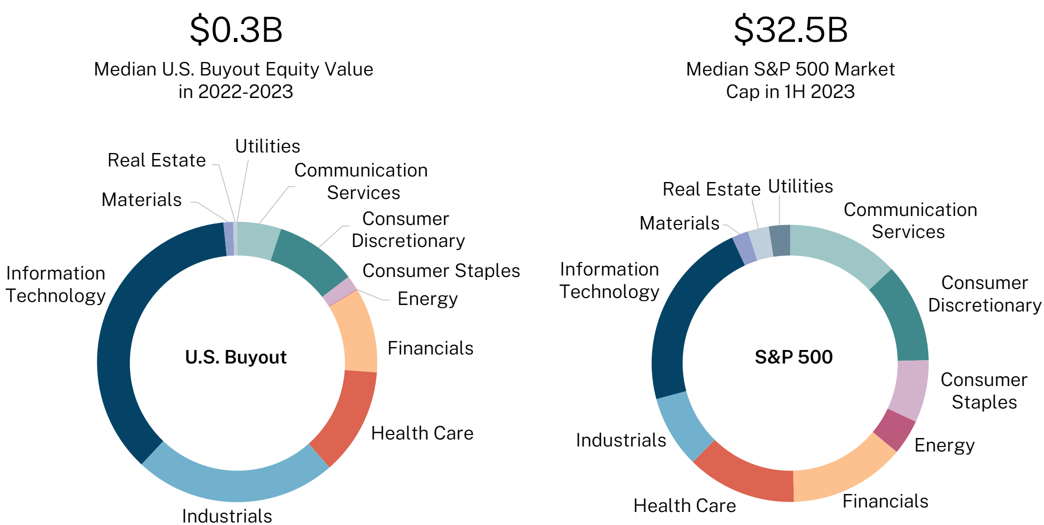
Source: Hamilton Lane Data, Bloomberg (December 2023)

This is, in the end, the core of the reason private markets outperform. It's not about magical financial engineering or wizardry around leverage. It's about boring operational performance. The outperformance in 2022, along with the continued performance in 2023, is a simple matter of stronger revenue and EBITDA than public companies. Throw out any sort of complaints and accusations you like, but there's no arguing with the data. The answer doesn't lie in the stars or in the fates, it lies in the numbers on the page.

Does this mean private equity investors are smarter than their public counterparts? Not necessarily, but the industry's governance is better, and the choice of companies is different and contributes to that better performance.

Chart 2.3: North America Buyout and S&P 500 Company Composition

By Sector and Count



Source: Hamilton Lane Data, Bloomberg (December 2023)

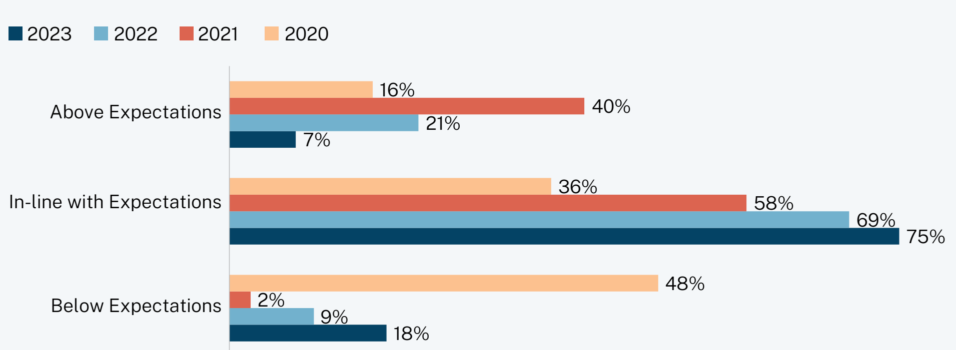
There are two key pieces of information in Chart 2.3:

- Buyout has generally avoided some areas that are more represented in the public markets and that were highly volatile and not very good performers, notably materials and consumer. Instead, buyout has generally been overweight in sectors that have shown greater growth and resilience during economic cycles, especically information technology and industrials.
- More importantly, the size of companies varies drastically, with an average company size of $32.5 billion in the S&P 500 versus $328 million in the buyout universe. The amount of control you can exert over a smaller company is enormous compared to a larger one.

Private equity's operational outperformance is closely tied to better sector selection and a greater ability to create paths for operational growth.

What are GPs' revenue expectations for their portfolio companies?

Chart 2.4: GP Survey – How would you describe revenue growth across your portfolio companies over the past year?



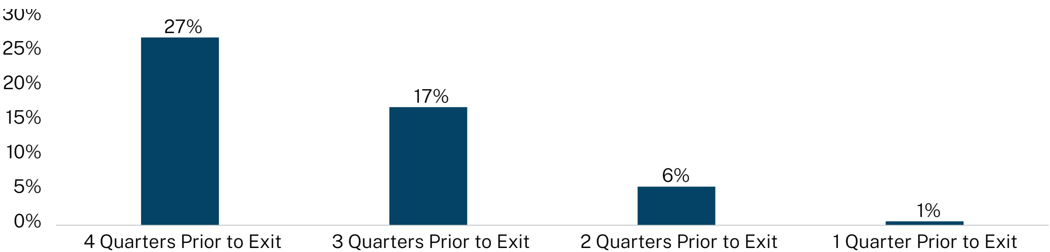
Source: Hamilton Lane General Partner Survey 2023 - 2024 (December 2023)

While revenue is growing roughly in line with expectations, the outperformers are shrinking, and the underperformers are rising. That will no doubt embolden those saying that valuations must fall. Perhaps. Or it may simply reflect a more difficult operating environment but one that is being handled, in the vast majority of cases, quite well. One interesting tidbit is that, when you ask GPs to look at rates of growth at individual companies, those with declining revenues are shrinking from a year ago, while those with outsized revenue growth are increasing from a year ago. Hmm, that seems like pretty good news to us.

For the sake of argument, let's momentarily accept the premise that valuations are inflated, that it's all an accounting game featuring nefarious general partners fiddling with the numbers. And we can prove it. The companies will be sold for something less than the valuation. You can't have one without the other, because no one will buy a company for more than it's worth, would they? (Well, Softbank would but let's assume they aren't buying every company in every private equity portfolio.) Let's even look at the period we just experienced where capital markets were lousy. Sale prices had to be less than valuations, didn't they? Let's look at data from the most important chart in this overview.

Chart 2.5: Median Exit Markups During the Year Prior to Exit

Deals Exited from Q2 2021 – Q2 2023



Source: Hamilton Lane Data (January 2024)

Can it be? Sale prices were HIGHER than those inflated valuations! 'Tis true and has been throughout private equity's history; the fact that it continues to hold true through the most recent bear market should make even the most skeptical among you reconsider your view.

Private Equity Can't Perform Well with Higher Interest Rates

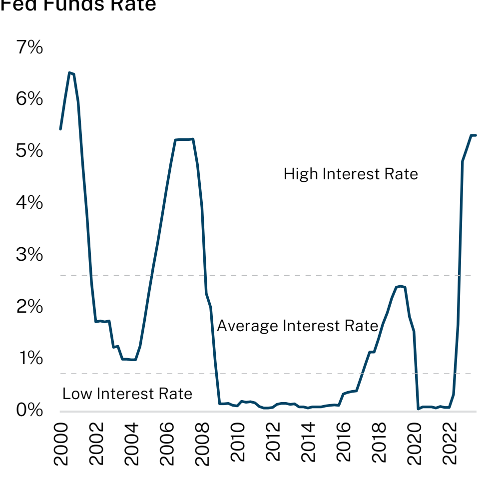
You've all heard this one. Private equity has done well only because interest rates were at zero. Now that rates are higher, returns are doomed. We love this one for so many reasons. Let's just think about this for a moment before we get to the data and facts.

This argument has, as its unspoken premise, the idea that private markets returns, particularly equity, are primarily driven by leverage and financial engineering. That premise we've already shown to be suspect, which is our polite way of saying it's complete nonsense.

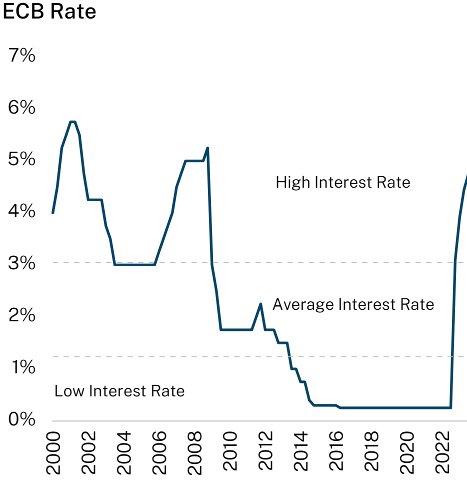
The argument also lives in a vacuum. But let's assume that it's true and that private assets returns decline with higher interest rates. Do we think public market returns will magically rise? It is equity whether it's public or private. Nothing like what's good for the goose not being good for the gander. (We confess we have no idea what that cliché really means but it seemed to fit in that sentence for some reason.)

Now for some numbers...

Chart 2.6: Interest Rates Over Time



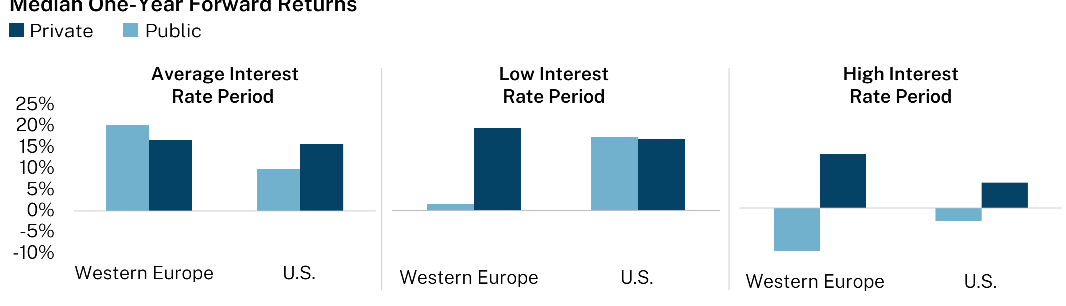
Source: FRED (January 2024)

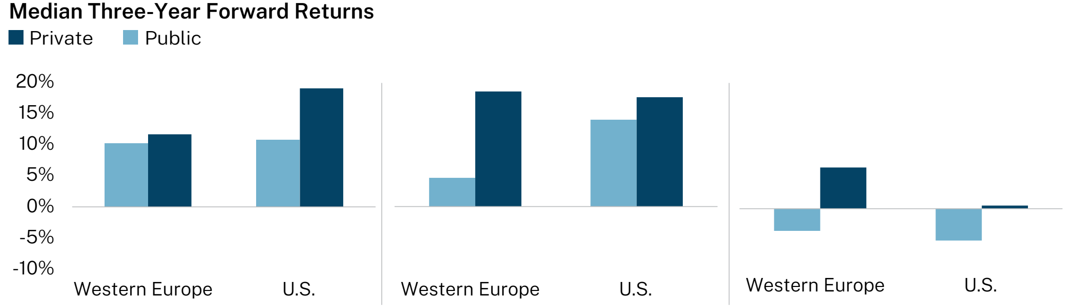


Source: ECB (January 2024)

We have divided interest rate regimes into three categories: high, average and low. Don't get hung up on the exact numbers, our model is plus or minus a half of a standard deviation of the average over the timeframe. (For those without a statistics degree, that splits the sample, roughly, into thirds.) Play with different models, the general context will be the same. We've then annualized median one-year and three-year returns across geographies and interest rate environments. What did we find?

Chart 2.7: Median One-Year and Three-Year Forward Returns





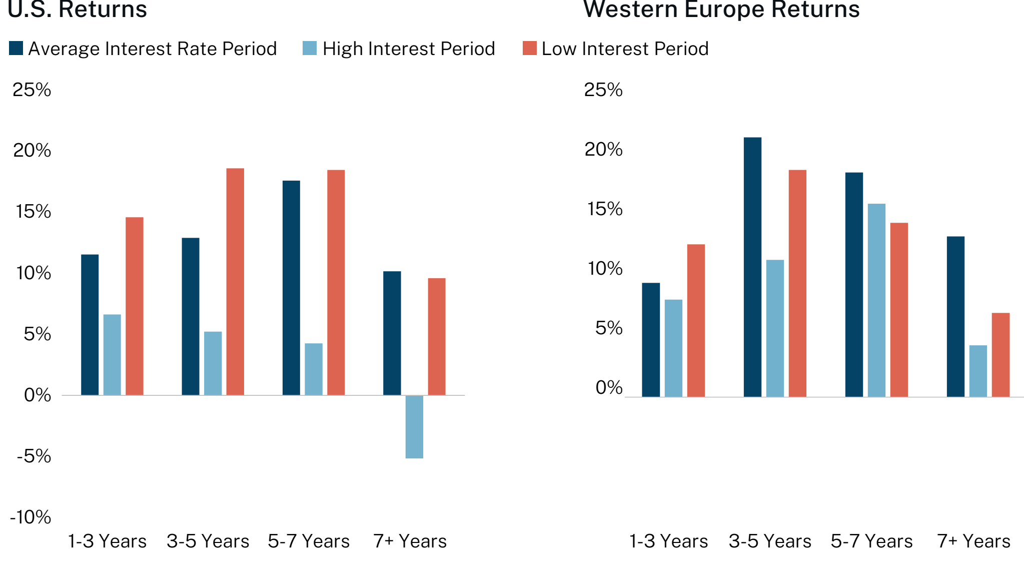
Source: Hamilton Lane Data, Bloomberg, FRED, ECB (January 2024)

The one-year numbers contain a lot of noise, but the best private markets returns have come during periods of average interest rates. The three-year numbers are subject to less noise and show a similar trend in the U.S., while European private equity fared best during lower rate periods.

At this point, the skeptics are saying, “Aha! Even Hamilton Lane’s data suggests that returns are lower during periods of higher rates. This is a terrible time to invest in private equity.” We concede that, at first glance, that appears a reasonable conclusion. But remember what we said about this argument living in a vacuum? Look at how public markets fared during those same higher interest rate periods. Negative in all cases. While *absolute* returns were lower, private equity still maintained its relative advantage over listed assets.

Things get more complicated the more you look at the data, but let’s keep going. What about forward, one-year private equity returns by the fund’s age? We care about this because where the fund is in its life might make a difference around sensitivity to interest rates.

Chart 2.8: Forward One-Year Private Equity TWR by Fund Age



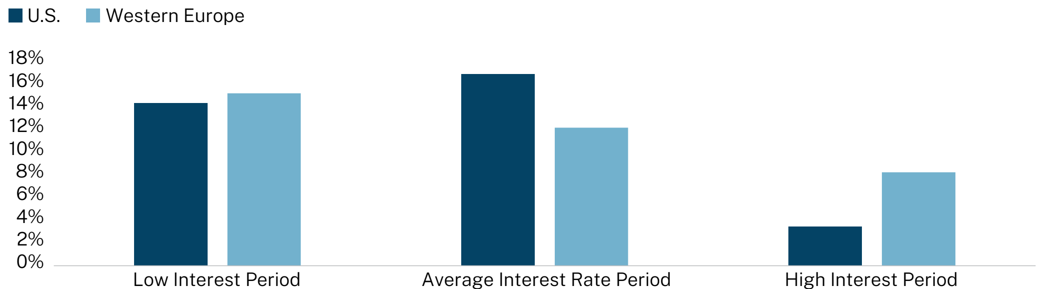
Source: Hamilton Lane Data, OECD, FRED (January 2024)

(Having this much data is pretty cool, is it not? If you don’t have similar data or access to someone who does, perhaps the bigger question to ask yourself is how exactly are you investing?) Analyzed this way, in the U.S., higher interest rate periods seemed to have more of an effect on funds in their harvesting periods than funds in their investment periods. Interestingly, European funds bucked that trend, with interest rates seemingly having little effect on five- to seven-year-old funds. This is likely driven by the European funds of the early aughts, which produced some of the region’s finest vintages.

We looked at it another way, by analyzing funds that were more than 50% invested in different interest rate environments.

Chart 2.9: Median Since Inception IRR by Interest Rate Period and Geography

Funds Invested > 50% of Capital in Interest Rate Period

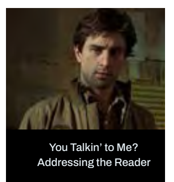


Source: Hamilton Lane Data, FRED, ECB, (January 2024)

This analysis follows what we saw from the prior chart. Funds that invested the majority of their capital in low interest rate periods performed better than those that invested in high interest rate periods. This is true across both geographies, although most pronounced in the U.S.

So, what do you make of this? We can hear many saying, "See, this proves that returns are better in low interest rate environments." Well, sort of.... What we see is that investing in a high interest rate environment will likely produce lower returns than investing in a low interest rate environment. High interest rate environments tend to coincide with bull market peaks and are often succeeded by significant recessions, a dynamic that is likely to create lower absolute returns. However, remember the picture from Chart 2.7. The three-year forward returns handily beat the public returns. If private returns are lower, so are public, and you are still easily outperforming your public returns.

Investing in a high interest rate environment will likely produce lower returns than investing in a low interest rate environment.


You Talkin' to Me?
Addressing the Reader

Let us speak candidly here. (Because we've shown such restraint until now...) What is particularly interesting is that your head continues to argue that returns are going to come down because the existing portfolio is going to be hammered by higher rates. Refinancing gets tough, cash flow is diverted to higher interest payments, it's all bad, and the bad things are only happening to private assets. Get your money out of private markets now: Stop committing to new funds, sell everything on the secondary market, list your holdings on the dark web, do whatever you need to do. That's where your head is headed, but that's not what the evidence shows. Sorry. It all sounds so intuitively obvious and is so neat a reason to stand back and ponder your investment options. "Let the damage happen," you're thinking. "Do nothing; be cautious; play it safe." But that's not what's happening in portfolios. It's the new deals that have lower returns, which makes sense given the higher cost of capital. The existing deals appear to do fine (not great by lofty private equity standards but fine enough to best listed assets). Cash? When was cash the best place to be over any extended period of time?

Let's look at something else that perhaps only interests us. How do multiples and interest rates relate, if at all?

Chart 2.10: Valuation Multiples and Interest Rates

Recession — North America Buyout EV/EBITDA — S&P 500 EV/EBITDA — Fed Funds Rate

EV/EBITDA: 0x, 5x, 10x, 15x, 20x, 25x
Fed Funds Rate: 0%, 1%, 2%, 3%, 4%, 5%, 6%, 7%, 8%, 9%
2004, 2008, 2012, 2016, 2020, 2023

Source: Hamilton Lane Data, Bloomberg, FRED (December 2023)

Lots of squiggles and lines in Chart 2.10 but you can see that, generally, multiples and interest rates don't have the kind of correlation you would have imagined or been told to expect. Multiples generally move in the same direction for both public and private, although there are large swings in either direction over shorter time periods. What is interesting to note is that, in the GFC, it took multiples around two years to recover even as rates dropped to zero. During the current period of interest rate increases, public multiples began dropping ahead of rate hikes and private multiples subsequently caught up with that drop but then have risen sharply in the last short period. While public multiples have also risen, the rise has not been as sharp as the private multiples. What should we make of this? Does it mean that private multiples will retreat soon? That public multiples will rise? That both have foreseen lower rates and will continue to rise? We're not sure, but we are reasonably sure that all the talk about rates determining multiples is just that: talk.

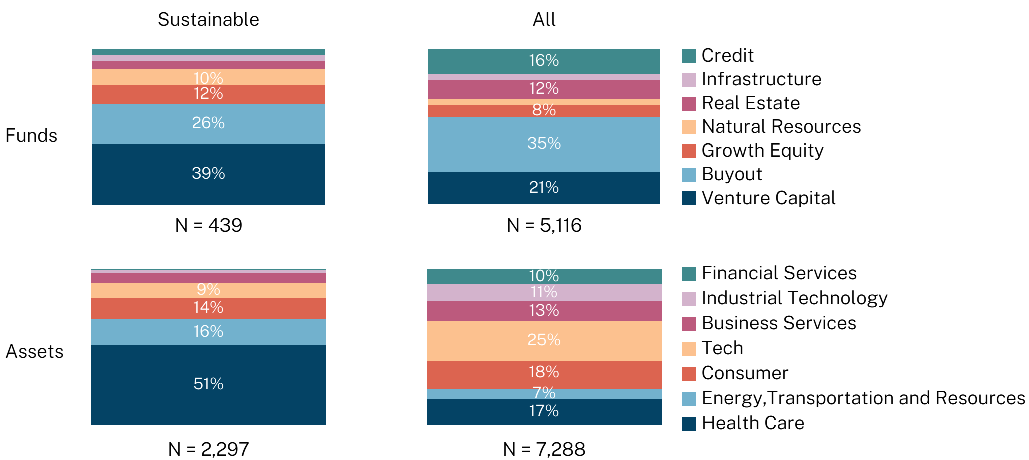
Focus on Sustainability Will Ruin Future Returns

"Give every man thy ear, but few thy voice; Take each man's censure but reserve thy judgment."
-Hamlet, Act I, Scene III, William Shakespeare

We know, we know… Mere mention of the word "sustainability" and we run the risk of moving into unsavory (and unwinnable) political debate here, but bear with us. The issue of sustainability as it relates to our investment choices is not going away, regardless of political leanings. One of the arguments against it relies on the assumption that investments predicated on sustainability are, by definition, lower-returning investments than those that are not. There's a lot of confident talking about that conclusion, but you know our feeling about confident talking (unless we're the ones doing that talking, of course).

For this analysis, we used the UN SDGs for what constitutes a sustainable investment. You can argue that definition, but it is generally used and it's a start. We then compared the constituent parts of sustainable investments to those of all private equity.

Chart 2.11: Addressable Market

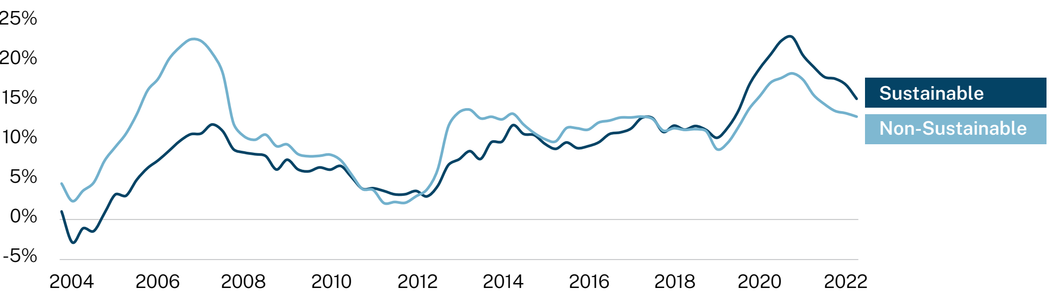


Source: Hamilton Lane Data (January 2024)

The color coding helps make a few things immediately apparent. One is that a large proportion, more than one-third, of sustainable investments is in the venture sphere. That percentage is more than double venture's overall market share. Seems an important fact to keep in mind as you build a sustainable portfolio in today's environment. The second thing is the enormous proportion of healthcare investments that comprise more than half of sustainable investments and triple what that sector represents in the private markets universe. Now it gets interesting.

Chart 2.12: Rolling Fund Performance

Five-Year Rolling TWRs

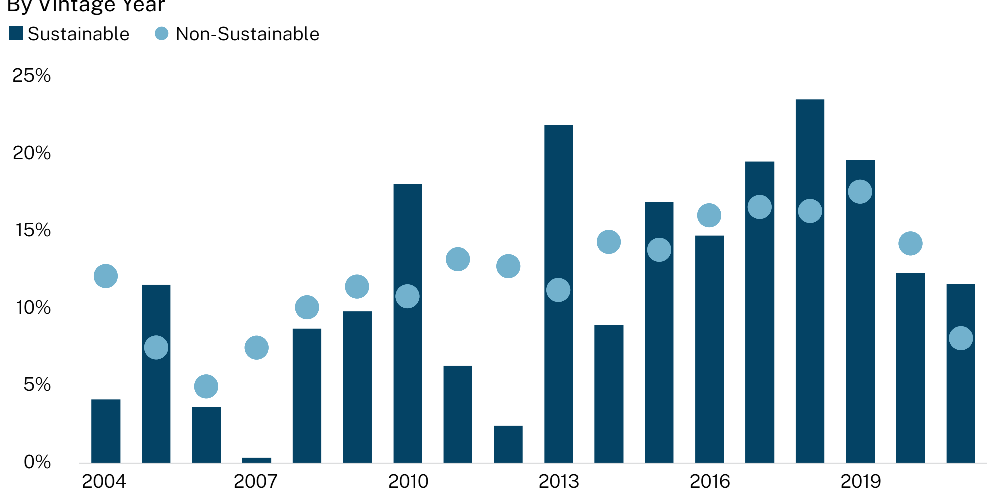


Source: Hamilton Lane Data (January 2024)

Sustainable investment trailed behind non-sustainable investment for much of the aughts and early teens, which apparently is when conventional wisdom stopped looking at data. The last five or six years have seen that trend change meaningfully. That may be a function of venture and healthcare doing well in that period or a sign of a more mature market. But it is hard to ignore. (Unless you are choosing to ignore it for political reasons, in which case data is unlikely to sway you.) We observe the same pattern in funds, with those having a sustainable focus doing better more recently.

Chart 2.13: Fund Net IRRs

By Vintage Year

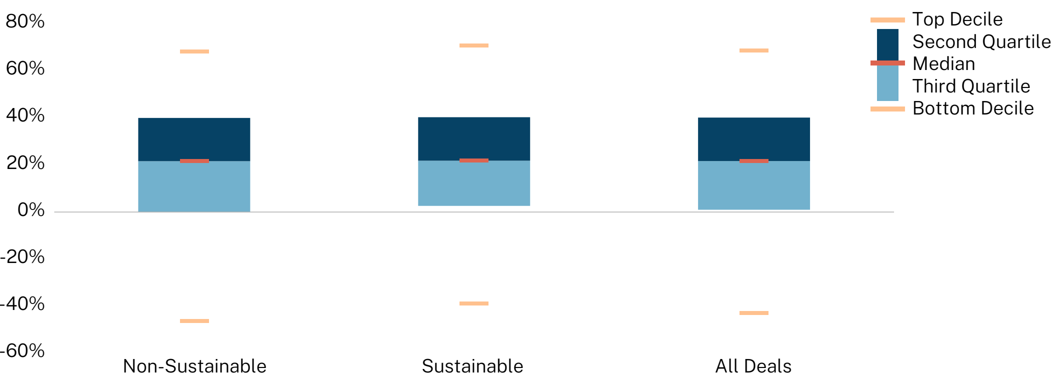


Source: Hamilton Lane Data (January 2024)

However, looking at Chart 2.13, it's easier to see why the sustainable fund universe has a lot of history to overcome. Some of those early IRRs relative to the rest of the industry are discouraging, at best. But the story is quite different when you look at deal-level returns.

Chart 2.14: Dispersion of Gross Deal IRRs

Realized Deals Only, Deal Vintages 2010 – 2020



Source: Hamilton Lane Data (January 2024)

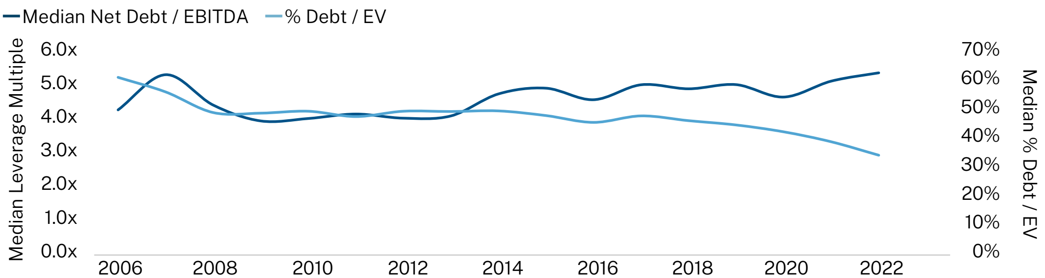
The return differential is much smaller across sustainable and non-sustainable deals. This fits with our overall view that sustainable investing will become mainstream and there won't be a different portfolio set called "sustainable funds." As investors recognize that, in fact, sustainable deals have quite similar return profiles, they will become more common in portfolios. Right now, however, investors focused on sustainability will need to recognize the portfolio shift that focus will entail. There is no evidence that future returns will be reduced by any focus on sustainable investing. Put that one in your busted myth category.

There's Too Much Leverage in Portfolios, and Returns Will Suffer

If we had a dollar for every time we've heard this one over the last 30 years.... It's the argument that just won't go away and instead gets trotted out to justify all sorts of inaction and avoidance of private markets. Today, it is based on the premise that higher rates, coupled with higher leverage, means we're doomed. Let's try to agree on the leverage levels we have in the markets.

Chart 2.15: Buyout Median Leverage Multiple at Acquisition

Deal Years 2006 -2022

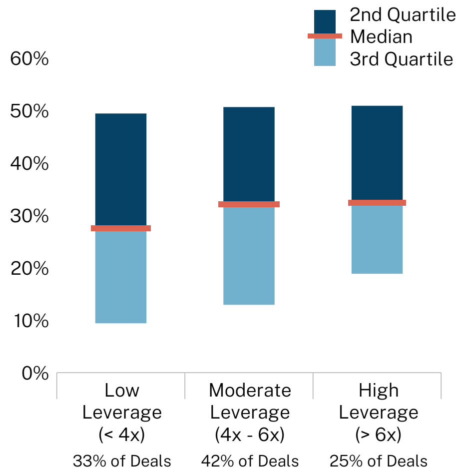


Source: Hamilton Lane Data (November 2023)

Sure, there's been a slight upward trend recently (there would be with zero interest rates), but we haven't moved a whole lot over the last 15 years. In fact, if you measure debt as a percentage of enterprise value, there's been a steady decrease over that same time period. Yes, there's leverage, but is it excessive? The evidence says no. But that's only part of the story. Let's look at returns over the last 10 years and leverage levels.

Chart 2.16: Realized Buyout Deal IRR Quartiles by Leverage

Deal Years 2012–2022



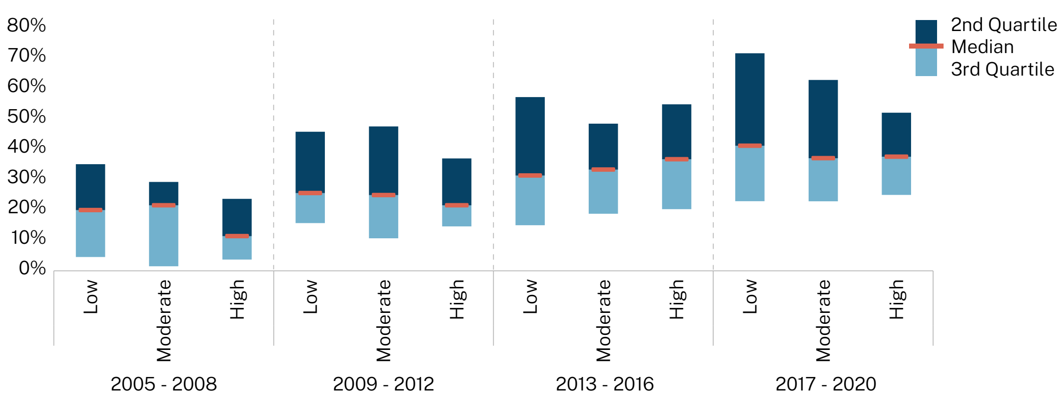
Source: Hamilton Lane Data (November 2023)

Be honest, who saw that one coming? Perhaps you expected returns to be roughly the same (and you could argue that it makes lower leverage deals better because of the lower risk profile), but did you honestly expect dispersion of return to be less with higher leverage? We didn't since we assumed higher leverage meant more risk and a more binary outcome with more losses. We are as cynical as you are and can hear the whispers, "Well, sure Hamilton Lane, what would you expect in a zero-interest-rate environment that you have presented using data over the last 10 years."

Fair. So, let's look across different cycles.

Chart 2.17: Realized Buyout Deal IRR Quartiles

By Leverage and Deal Year Groupings



Source: Hamilton Lane Data (January 2024)

Doth mine eyes deceive me or is there a significantly lower dispersion range for highly levered deals across all cycles save one? Fascinating. Returns don't appear to be consistently better for one level of leverage versus another. Sure, pre-GFC, high leverage levels hurt returns, but is that an environment we believe will return? Interestingly, while lower leverage produced better returns, it was not so much better that you can conclude you shouldn't be using leverage. Let's look at it with our least favorite type of chart.

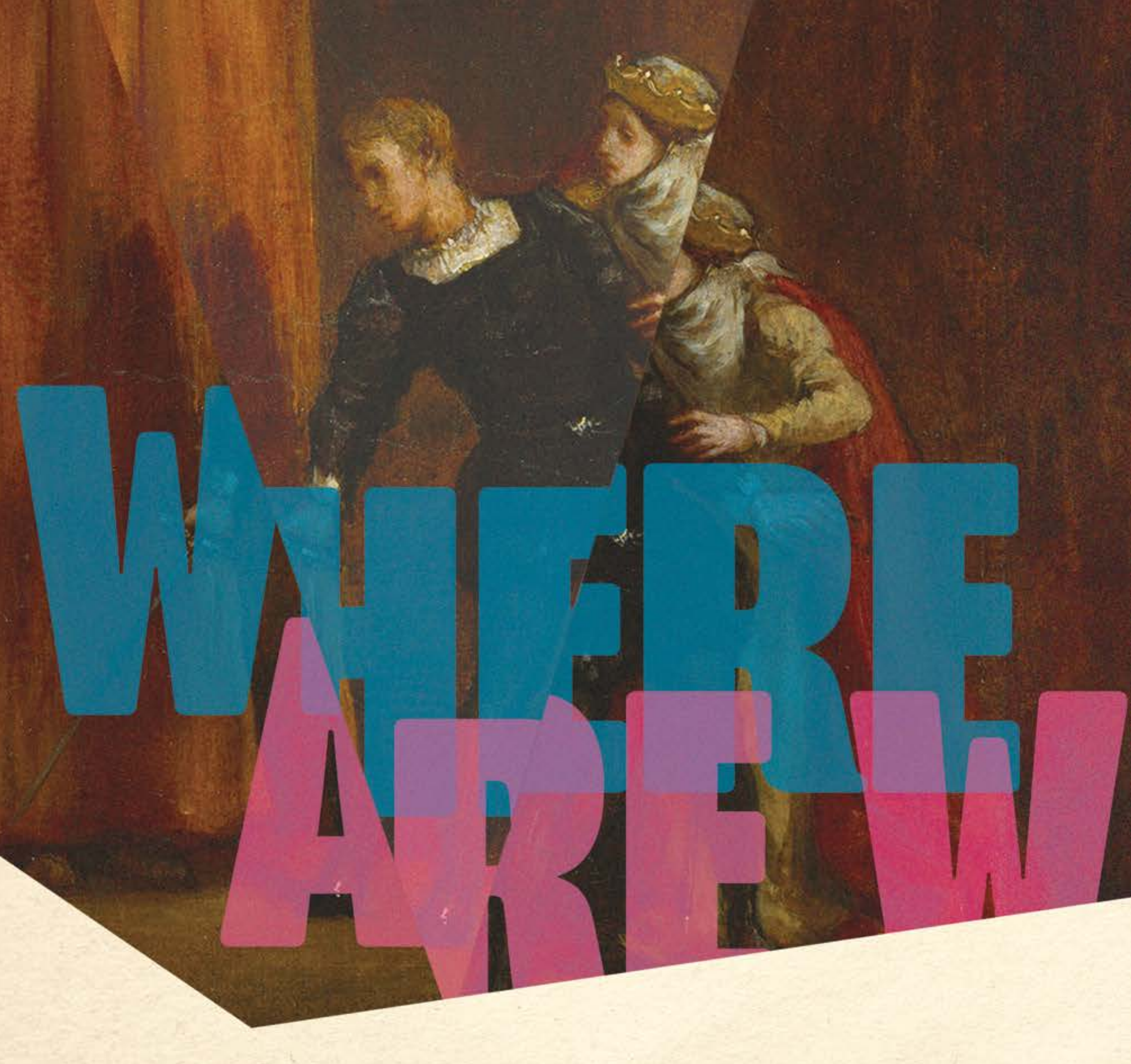
Chart 2.18: Deal Leverage vs. Gross IRR

Gross IRR
200%
150%
100%
50%
0%
-50%
-100%
-150%
0.0x 1.0x 2.0x 3.0x 4.0x 5.0x 6.0x 7.0x 8.0x 9.0x 10.0x
Leverage Multiple

Source: Hamilton Lane Data (November 2023)

No, we aren't trying to plot the stars in the Milky Way. Scatter charts do allow us to look at a wide spread of deals and their returns plotted against gross IRR on one axis and leverage multiple on the other. If leverage were the determining factor, or even a particularly important one, you would see the stars in the Milky Way gathering in the lower right portion of the chart. This is a random smattering of dots.

Where chaos rules in scatter charts, you have no correlation. If you think returns in private markets are going down, alluding to leverage may have an emotional appeal, but it has little empirical basis.



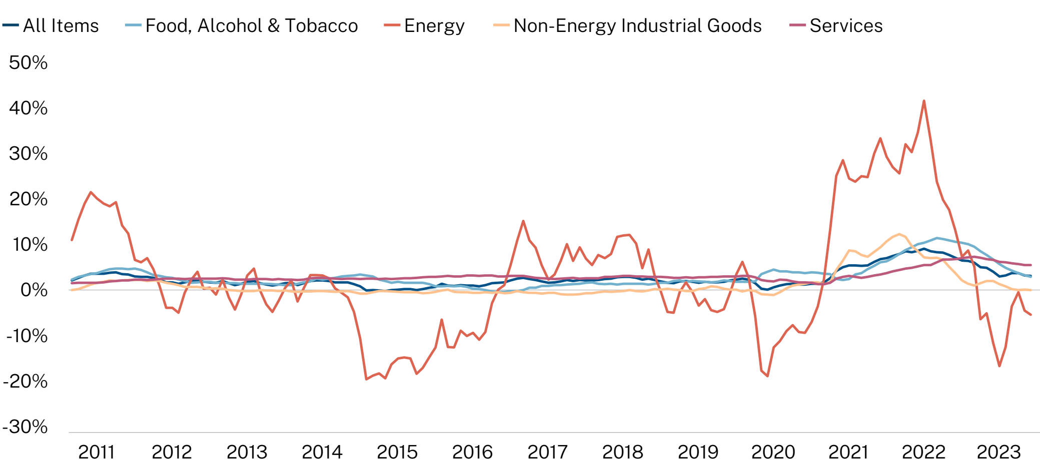
Where Are We Now?

e have been justifiably proud of our macro market predictions over the years. Some might say we have even gloated about our accuracy, particularly around economic growth trends, up and down. (Ok, ok, so we've been a little self-congratulatory, but we have lots of other nice qualities!)

So, how did we do in our 2023 market overview predictions? In a word…well, two words:

But let's not be so negative and instead start by taking a look at what we got right: Inflation.

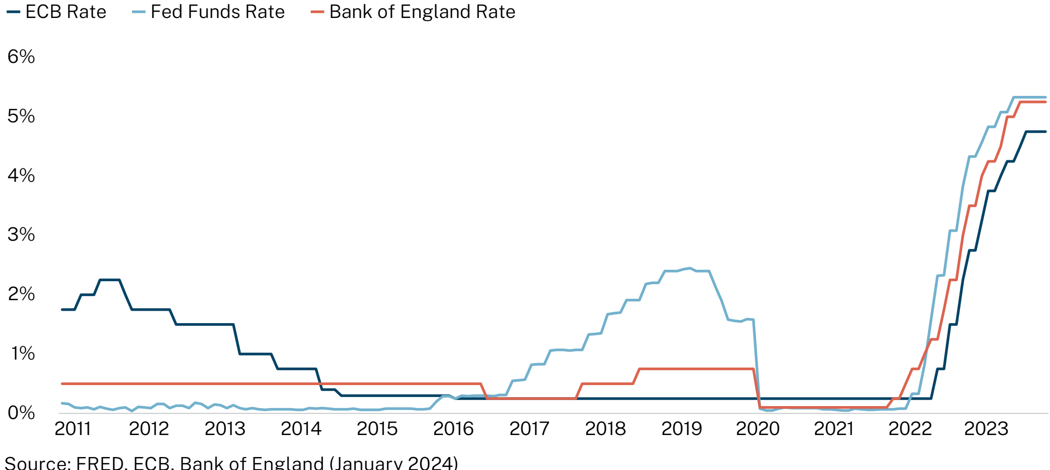
Chart 3.1: **U.S. Inflation**



Source: U.S. Bureau of Labor Statistics (January 2024)

We thought inflation was a supply side-driven phenomenon and that it would decrease more rapidly than people anticipated at this point last year. We got that right. The drop in inflation is as rapid as the rise was two years ago and we see the same chart pattern in most economies. We were also somewhat right about interest rates. ("Somewhat," in the artful world of economic forecasting, is the same as being 100% accurate so we'll embrace the ambiguity.)

Chart 3.2: **Central Bank Rates**

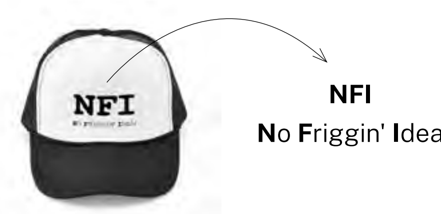


Source: FRED, ECB, Bank of England (January 2024)

We said that the Fed would keep raising rates and probably not stop until the second quarter of 2023. Close enough. As we have all learned, the Fed's rate rise was the most rapid of any over the last 30 years. Alas, that is where our Nostradamus Award was pulled away. We thought the higher rates would lead to a recession in the U.S. and Europe.

They didn't. Not even close.

We failed to anticipate the reduced impact of higher rates on the U.S. consumer, in particular. We failed to anticipate the resilience of consumers globally. We failed to anticipate the desire to spend on experiences after the pandemic. (Though in hindsight that one seems forehead-slapping obvious.) So where does that leave us today? We'd like to introduce our awesome new HL hat that provides the answer.

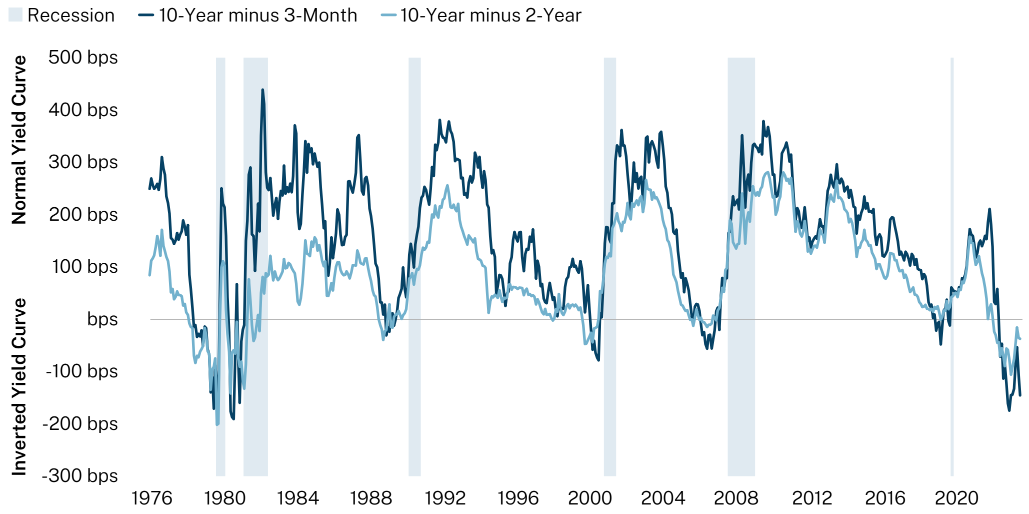


This is a tough macro call this year. Very tough. But we'll offer our best probabilities. We remain skeptical that inflation will come back. We are reasonably convinced the supply chain issues are generally resolved. We respectfully disagree with the stock markets' judgment, globally, that the worst of the economic times are behind us. We suspect that the Fed and the ECB, in particular, will be as wrong about inflation going down as they were about inflation going up, and they will keep rates too high for too long and cause an economic downturn. We also remain devotees of the yield curve indicator.

Chart 3.3: **Yield Curve**

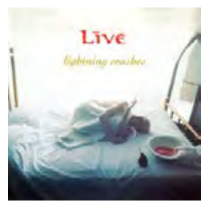
10-Year Treasury Spreads

Against Two-Year and Three-Month T-Bills



Source: Bloomberg, FRED (January 2024)

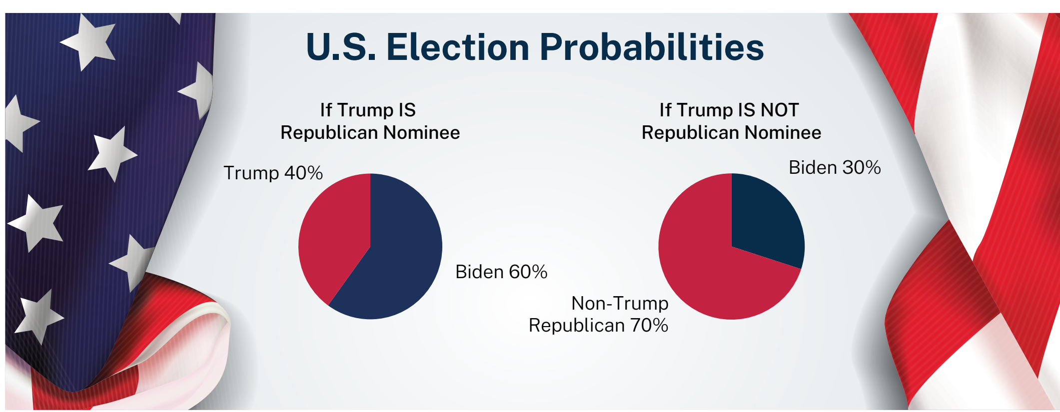
We aren't prepared to throw out an indicator that has been correct for decades. With all those caveats and hedges, we will predict here that the U.S. and most of the industrialized world will slip into recession or near recession later in 2024. With that said, and knowing how much we hate hedging, we have to say that the next most likely probability is that we do have a soft landing and that the global economy, particularly that in the U.S., is closer to what we experienced in the mid-1990s. Go look at that period. The Fed had raised rates, and everyone feared a recession. Instead, what transpired was a strong economic environment for the next five years until the dot-com bubble burst. While not our highest likelihood outcome, this is a real possibility; it's one the global markets are predicting, and they have been right far more often than most pundits. Fun fact: The top-selling rock song in 1995 was...



The Politics of 2024

There are a lot of very important elections happening in 2024 that will have a real impact on investments. How important? A recent *Forbes* article summarized the impact quite well: “More than 50 countries around the world with a combined population of around 4.2 billion will hold national and regional elections in 2024, in what is set to be the biggest election year in history featuring seven of the ten most populous nations in the world.” Mexico, Indonesia, India, Taiwan, the European Parliament, the UK, Finland, India, Russia (sorry, had to see if you were awake), and, arguably the most important economically, the U.S. Leaving aside our bias as to whom we hope wins the U.S. election, we’ll focus solely on the current odds and what the impact of different scenarios will be from an economic standpoint.

Political Prediction



Our view is that Trump is likely to be the Republican nominee and Biden the Democratic nominee. In that scenario, we believe Biden has a 60% chance of winning the election. Our view is that the result is effectively a reflection of the general electorate’s view of Trump, because this is a year when we believe that the Republicans should easily defeat Biden, who is viewed as simply too old to govern. No matter that Trump is almost as old since perception is reality, and Biden looks far more frail than Trump. Our view is that if the Republicans nominated anyone other than Trump (well, assuming it’s not another MAGA acolyte), the Republicans have a 70% chance of winning the presidency. That’s an amazing swing.

“To argue with a person who has renounced the use of reason is like administering medicine to the dead.” - Thomas Paine

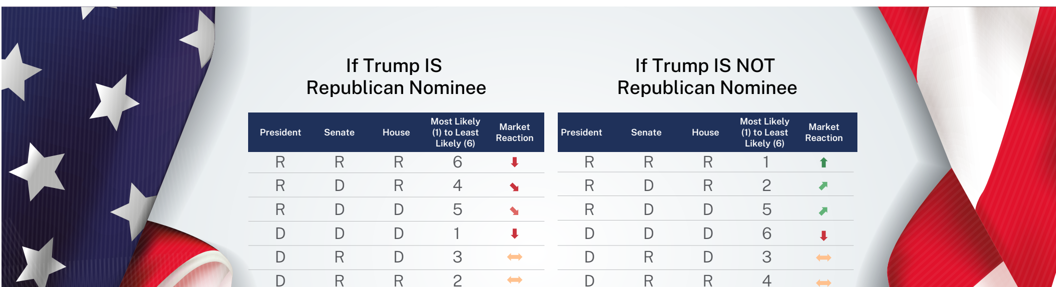
Ok, you say, that is current conventional wisdom. Well, Biden's odds at 60% are higher than what current polls indicate, but recall polls indicated a Republican sweep in 2022 and, when people found themselves in the voting booth, pulling that lever for a Trump candidate proved too hard. That's why we're at 60% for Biden against Trump. But is it really a foregone conclusion that the U.S. will run two 80-year-old candidates that few Americans appear to want on the ballot? Let's offer some considerations about what might happen that could change that calculus.

1. Biden knows he is politically weak but does not want to become a lame duck and have the party go through a convulsive primary, particularly so late in the process. He wins the nomination, then steps down and lets the Democratic Party select a candidate at the convention. Messy, never been done, but we'll give this one a 15% chance of happening. That Democrat, whomever he or she is, would have a struggle against Trump because they will not have gone through any election process. We'd still rate them a favorite to win. (Unless it's Kamala Harris, who would likely lose with too much Biden baggage.)
2. Trump is disqualified or imprisoned because of one of the many legal claims he faces. This is perhaps a slightly higher probability, but still only about 20%. The Republican Party has been unable to abandon Trump and it will take a court disqualifying him and that seems very unlikely. (We know, it's amazing that the party would not do anything if their candidate was campaigning from prison.) As we note, in this event, a candidate like Haley has very high odds of winning an election against Biden or almost any other Democrat.
3. Trump or Biden are incapacitated or die before the election. It sounds ghoulish to discuss, but it can happen. This is a variation of numbers 1 and 2.
4. A third-party candidate wins enough votes to become the swing factor in deciding the presidency. The U.S. system doesn't really work that way and throws the election, in most contested situations, to the House of Representatives. If it's anything like the current House, it has shown itself unable to decide anything that involves a serious issue, so it is difficult to know how this would turn out other than a constitutional crisis that makes its way to the Supreme Court. This is a chaotic outcome and has a less than 10% probability, but that's more than zero, isn't it?

Is it really a foregone conclusion that the U.S. will run two 80-year-old candidates that few Americans appear to want on the ballot?

What is the likely global financial market reaction to the U.S. election results?

Global Capital Markets Reaction to U.S. Elections



If Trump IS Republican Nominee

President	Senate	House	Most Likely (1) to Least Likely (6)	Market Reaction
R	R	R	6	⬇
R	D	R	4	↘
R	D	D	5	↘
D	D	D	1	⬇
D	R	D	3	↔
D	R	R	2	↔

If Trump IS NOT Republican Nominee

President	Senate	House	Most Likely (1) to Least Likely (6)	Market Reaction
R	R	R	1	⬆
R	D	R	2	↗
R	D	D	5	↗
D	D	D	6	⬇
D	R	D	3	↔
D	R	R	4	↔

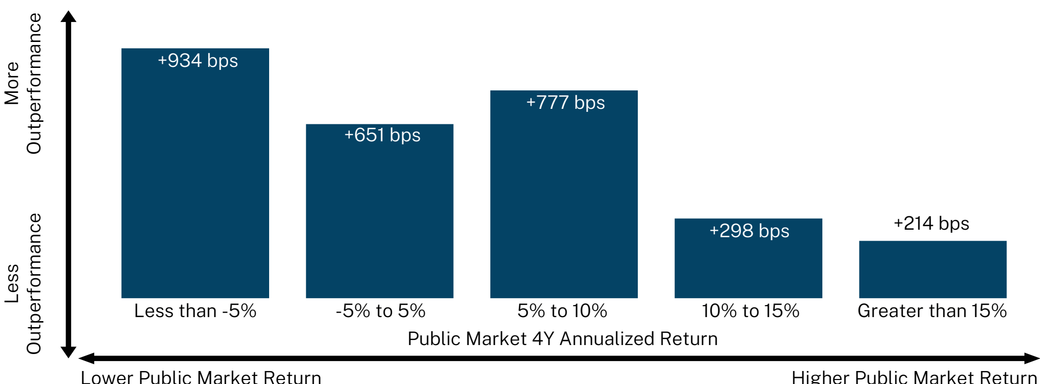
We won't go over all the numbers, but our view is that a Trump victory will result in real market declines globally. We don't say this as a reflection of Trump's policies or people around him; it is simply a view that markets view a Trump presidency as too unpredictable and unstable, and markets hate that kind of environment more than any other. This is very much at odds with traditional responses that favor a Republican administration.

Of course, if the Democrats win the presidency and Republicans have some control of one of the other branches of government, the markets will be flat. That's the situation we're in today. A Democratic sweep will result in market declines at the outset with a view that taxes and regulation will undoubtedly increase. A non-Trump Republican victory will likely mean higher stock markets globally with the belief that it will be a far more benign regulatory and business environment.

What if we told you that, while the macro picture matters a lot, it matters more in terms of the extent to which your private investments will outperform, not whether they will outperform. You'd hug us and send us flowers and chocolates. The good news is that it is exactly what we are going to tell you. (Please direct all floral deliveries to one of the office addresses appearing at the end of this book.)

Chart 3.4: Performance by Public Market Regime

All Private Equity Average 4Y Excess Return By S&P Return Regime

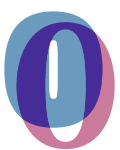


Source: Hamilton Lane Data via Cobalt, Bloomberg (January 2024)

In Chart 3.4, we are looking at average private equity returns (we'll repeat: AVERAGE, not top quartile) compared to four-year (or the length of one U.S. presidential term) public market returns over different public return environments. The point is simple: Whatever you think the macro environment will be doing over the next couple of years, history tells you that private equity will outperform the public markets. You think we're in trouble and going down more than 5%? Got you covered. Covered by more than 800 basis points of outperformance in fact. Perhaps unsurprisingly, the worst outperformance is when markets are booming, up more than 15%. But, if that happens, we're all drinking champagne and eating bonbons anyway, so who cares?

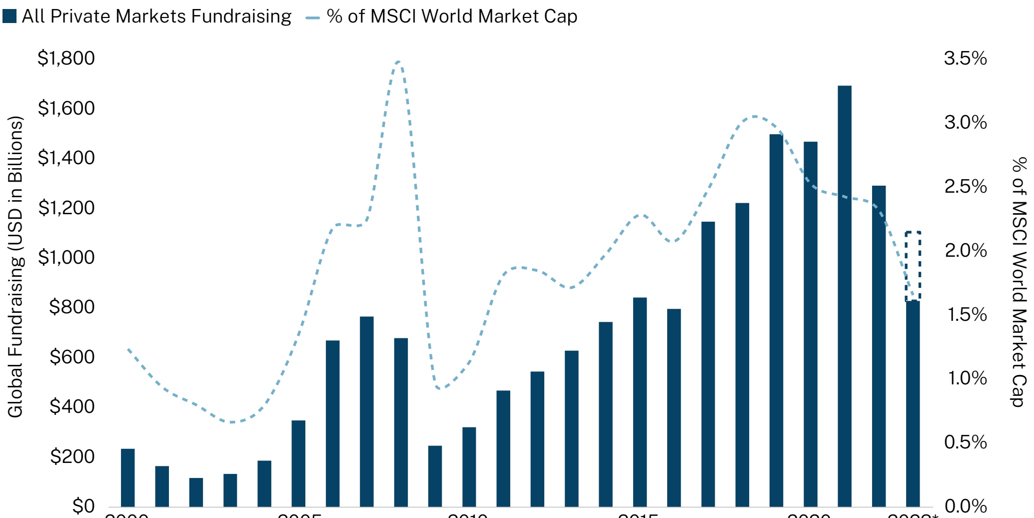
Whatever you think the macro environment will be doing over the next couple of years, history tells you that private equity will outperform the public markets.

Fundraising



k, so we need to fess up to something. We lied to you earlier on. Something is, in fact, rotten in the state of the private markets. It's fundraising.

Chart 4.1: Global Private Markets Fundraising

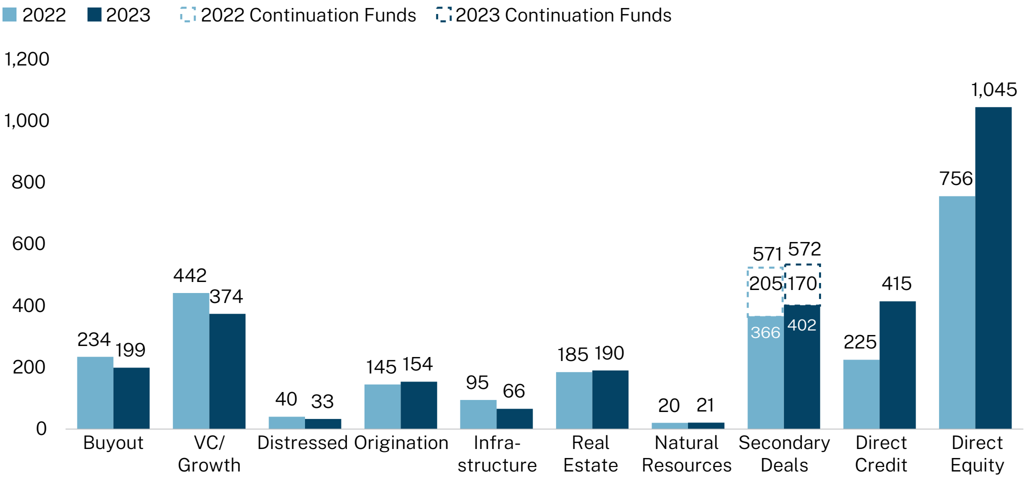


Source: Hamilton Lane Data, Pitchbook, Cobalt (January 2023)
2023 fundraising estimates annualized from Q3
Excludes fund-of-funds, secondary fund-of-funds, co-investment funds and core real estate

Then again, on a relative basis, it doesn't look so bad, does it? 2023 looks like it will be the seventh biggest fundraising year in history. But viewed the way every general partner on Earth looks at this data, the numbers are devastating. Fundraising is down around 35% from peak levels and it's down for the second year in a row. Levels are back to where they were in 2017, and the industry is quite a bit larger than it was in 2017. At least demand for capital from general partners is greater than it was then. Still, not a pretty picture.

There has been some reaction: Fund opportunities have generally gone down. Yet, direct transaction opportunities have risen.

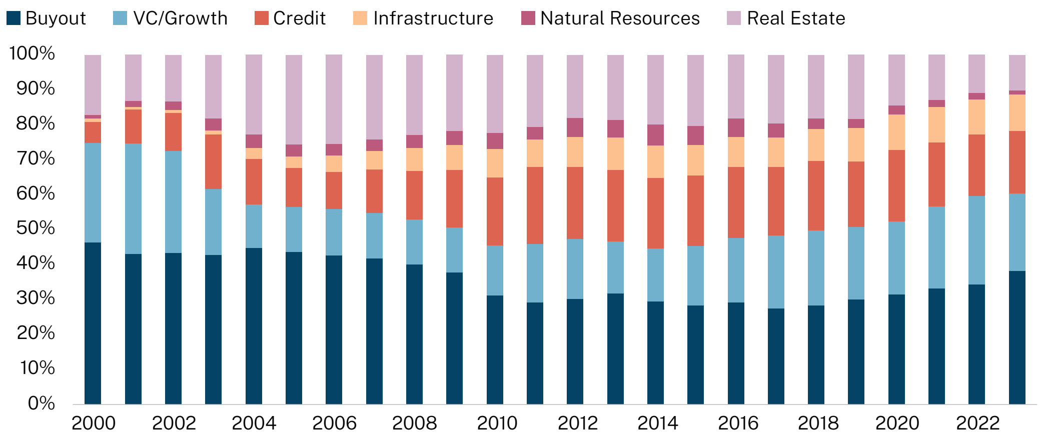
Chart 4.2: Private Markets Opportunities by Strategy



Source: Hamilton Lane Diligence (January 2024)

This likely reflects that general partners are more willing to partner to alleviate both their own capital needs and defer the day they need to re-enter the nuclear winter of fundraising. Interestingly, against a broader timeframe, the trend toward increased market share by equity strategies, particularly buyout, continues. (Let's be clear about what's happening: The total size of the industry is growing, and equity is re-taking market share. But the absolute capital flowing into credit and real assets has increased though the percentage is down.)

Chart 4.3: Trailing Three-Year Private Markets Fundraising By Strategy



Source: Hamilton Lane Data, Cobalt, and Pitchbook (January 2024)

Against all this growth in the industry, what is remarkable is how little geographic market share has changed. Look at the trailing, three-year numbers over the 10 years during which the industry more than tripled.

Chart 4.4: Trailing Three-Year Private Markets Fundraising by Geography

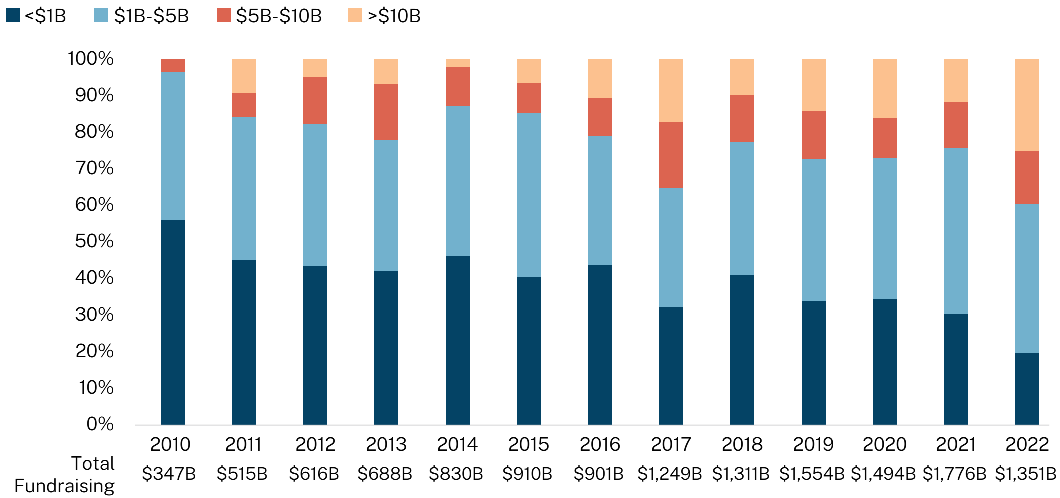
North America, Western Europe, Asia, Global, ROW

$1.3 Trillion
$4.5 Trillion
100%
90%
80%
70%
60%
50%
40%
30%
20%
10%
0%
5%
25%
10%
13%
48%
22%
9%
16%
51%
2012 Global Fundraising
2022 Global Fundraising

Source: Hamilton Lane Data, Cobalt, and Pitchbook (January 2024)

I doubt that we would have predicted that kind of stability if we were asked to draw this chart a decade ago. Here's one shift that we could have predicted – nay, did predict, but were told continually that we were wrong.

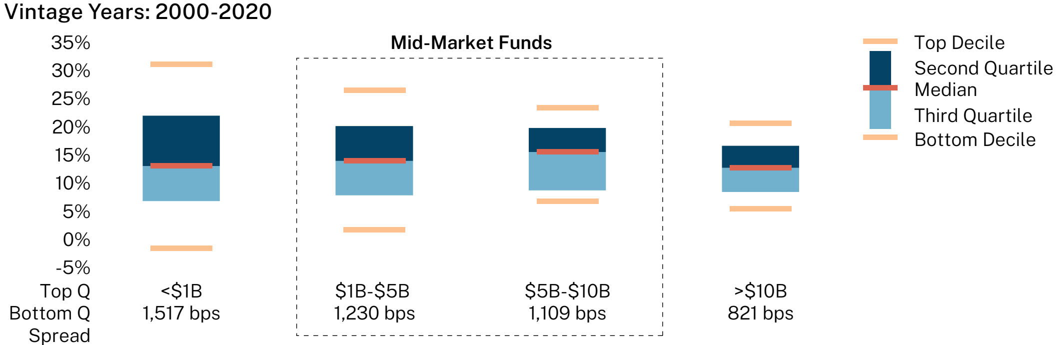
Chart 4.5: Share of Fundraising by Fund Size



Source: Hamilton Lane Data, Cobalt, and Pitchbook (January 2024)

Yup, the big get bigger and the small stay small. We have listened for years to the refrain, screamed with religious fervor, that large funds were bad, large funds had poor returns, large funds were not the future of the private markets industry. Well, it turns out that large funds weren't bad, large funds didn't have poor returns, and large funds are the past, present and future of the industry.

Chart 4.6: Buyout Spread of IRR by Fund Size



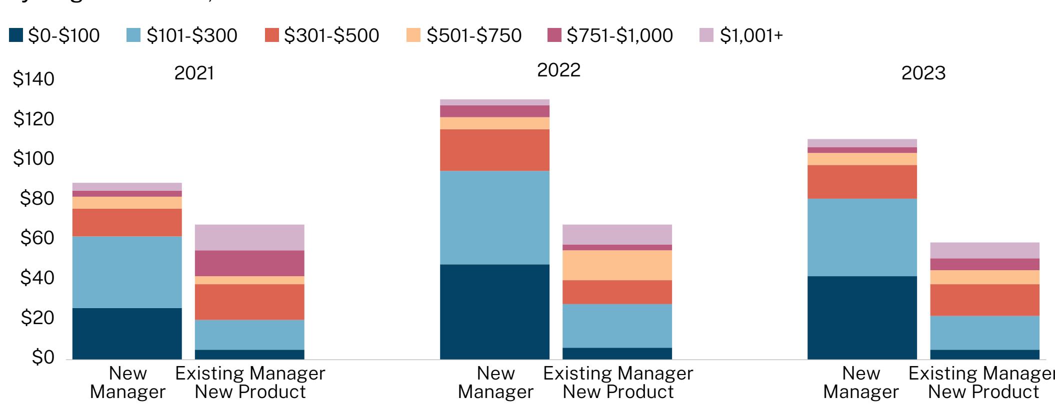
Source: Hamilton Lane Data (January 2024)

Why did anyone think that the private markets would be different from every other industry, including the asset management industry, in which size and scale matter? Here's a prediction we are confident in making: The private markets will continue to be dominated by the larger players. Period.

Here's where the industry is not like others. With a challenging fundraising environment, you would expect to see a dramatic reduction in the number of new fund managers seeking capital. Yes, we know how lucrative it is to land any capital but, surely, it hurts to beat your head against a wall in the private funds industry as much as it hurts in any other?

Chart 4.7: First-Time Fund Launches

By Target Fund Size, USD in Millions



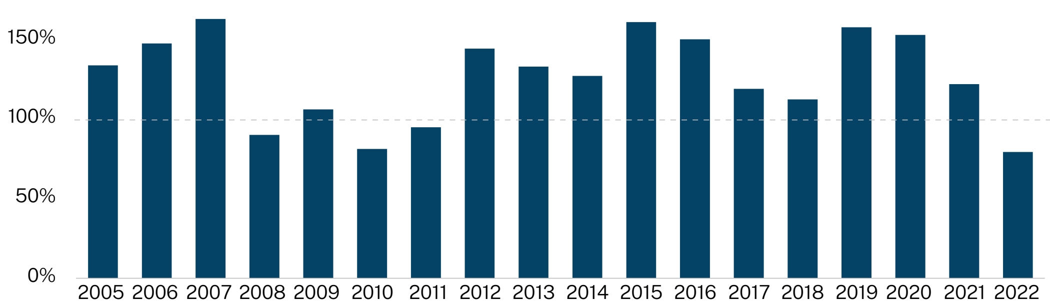
Source: Hamilton Lane Data (October 2023)

Then again, maybe it doesn't hurt that much. The number of new managers exceeds what we saw in 2021, a peak year for fundraising. Existing managers are also pretty bullish about launching new products. But note the difference in scale, because this is important.

Consider the size of the funds being raised in each category and then think back to the prior chart. New managers are raising the majority of funds at the very smallest end. That's the part of the market that is shrinking on a relative basis. Sure, many of these funds are focused on niche strategies, but what are the chances of success here? What are the chances that these funds will be funded and, once raised, do well? (Yes, we know in Lake Private Equity Woebegone, all small funds have 100% IRRs. In our database of actual results, however, they do not). Notice the difference in size goals for the existing managers' new funds. Much larger. In addition, those new funds have existing infrastructure to support a smaller size. Again, we see the larger industry players getting bigger, particularly through the growth of new product lines.

Let's return to the depressing (if you are a general partner) side of the business today. We know that the target size for funds are a combination of dreams, marketing and luck, but, in the aggregate, it gives you a good feel for what's happening out there when you see how funds are doing against their targets.

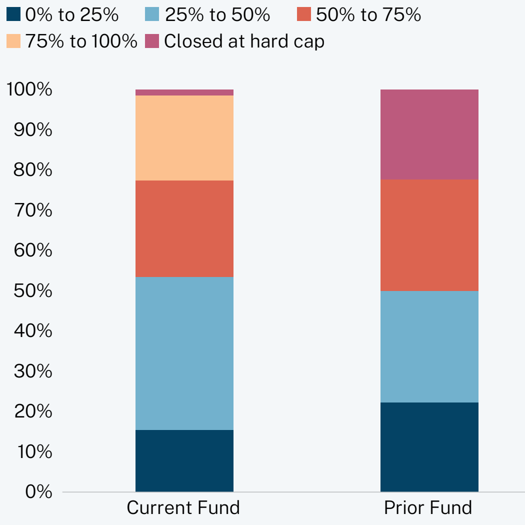
Chart 4.8: Buyout Fund Size as Percentage of Target Fund Size



Source: Hamilton Lane Data (December 2023)

Ruh-roh, general partners, not so good. The trend over the last three years is down, and 2022 marked the first time in 10-years that target sizes were not exceeded. In fact, 2022 fundraising was the biggest miss in 20 years. That is a hard statistic to ignore, even if you are a congenitally optimistic general partner. Let's get the numbers from the general partners themselves (and remember, these are our selected managers, so a relatively successful group compared to the overall private markets universe). First, we asked them how their first close looked compared to their target size and compared to their prior fund.

Chart 4.9: GP Survey – What % of target fund size did you close on at first close?
Current Fund 2022-2024 VY

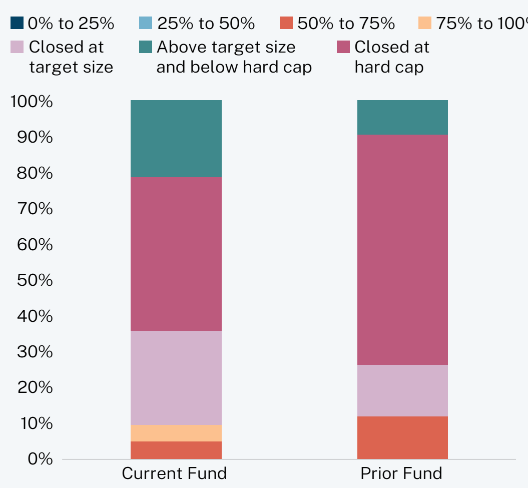


Source: Hamilton Lane General Partner Survey 2023–2024

Check out the difference in the pink shading today compared to the prior fund. No one is doing a one and done close. Look, these numbers aren't the kind that make anyone cry (other than those general partners), but they are striking for an industry accustomed to fairly routine fundraising over the last few years.

What about final closes looked at the same way?

Chart 4.10: GP Survey – What % of Target Fund Size Did You Close on at Final Close?
Current Fund 2022-2024 VY



Source: Hamilton Lane General Partner Survey 2023–2024

Once again, this is not bad on an absolute basis as funds are still being raised. But the percentage of funds not hitting the hard cap is up. Let's be real here: The hard cap is really the target number. This is private markets using retail marketing tactics. "Oh, we hit our hard cap, which is a number we never dreamed possible!" (Insert eye roll here). The target number is generally the "We did ok, but really wish we had raised more…" That puts these actual fundraising numbers into perspective. It's a tough world out there and we suspect, for a few more years, it will remain tough – oh and by the way, that goes for everyone. Remember our comment that the large will get larger?

Chart 4.11: Average Fundraising Length of Top 30 Buyout GPs

In Years

1.6
1.4
1.2
1.0
0.8
0.6
0.4
0.2
0.0

2012 2013 2014 2015 2016 2017 2018 2019 2020 2021 2022

Source: Hamilton Lane Data (December 2023)

Even the biggest and baddest of the lot are finding it more difficult to raise capital. Fundraising cycles are lengthening. Get used to it.

Well, jeez, that paints a bleak picture, doesn't it? We need help, dammit! We were born and bred to raise and spend! Where is our fundraising Batman to help us through these dark times?

If you listen to some, our Batman resides not in Gotham City, but in the Kingdom of Private Wealth.

Take a gander at some of these numbers. They're simply staggering.

- The private wealth management market in the U.S. is projected to wrap up 2023 at $58 trillion in AUM, up from $51 trillion in 2022. That is just under 50% of global private wealth management AUM, which is estimated to be $122 trillion by the end of 2023.
- The private wealth channel is extremely underpenetrated when it comes to alternatives exposure. Estimates by McKinsey put current allocations to alternatives at just 2% on average.
- If we just look at the average U.S. private wealth investor allocation, and it increased from 2% to 3%, that would add $580 billion to the AUM of the private markets. That's an increase in private markets AUM of more than 5%.

Interested? Are you not entertained at least?

We recently surveyed a global set of private wealth managers and asked them how much they planned to allocate to private markets in 2024 and whether this was a change from the prior year.

Chart 4.12: Hamilton Lane Private Wealth Survey: Allocation to Private Markets

Compared to 2023, this is an...	What % of your clients' portfolios do you anticipate allocating to private markets in 2024			
	None	1-5%	6-10%	10%+
Increase from last year	0.4%	18.2%	16.9%	35.1%
Same as last year	0.4%	6.9%	4.3%	16.5%
Decrease from last year	0.0%	0.9%	0.4%	0.4%

Source: Hamilton Lane Private Wealth Survey 2023 (December 2023)

In all fairness and transparency, this group represents many of our existing clients and partners, meaning there's a selection bias, because they are already interested and allocating to private markets. Still, when almost 75% of respondents are increasing their allocation from the prior year, in a time when the institutional fundraising market is weak, you can understand why there is so much interest in reaching the private wealth channel.

Empty the stage and leave a sole figure, Hamilton Lane, musing aloud as Hendrix's version of "All Along the Watchtower" purrs in the background.

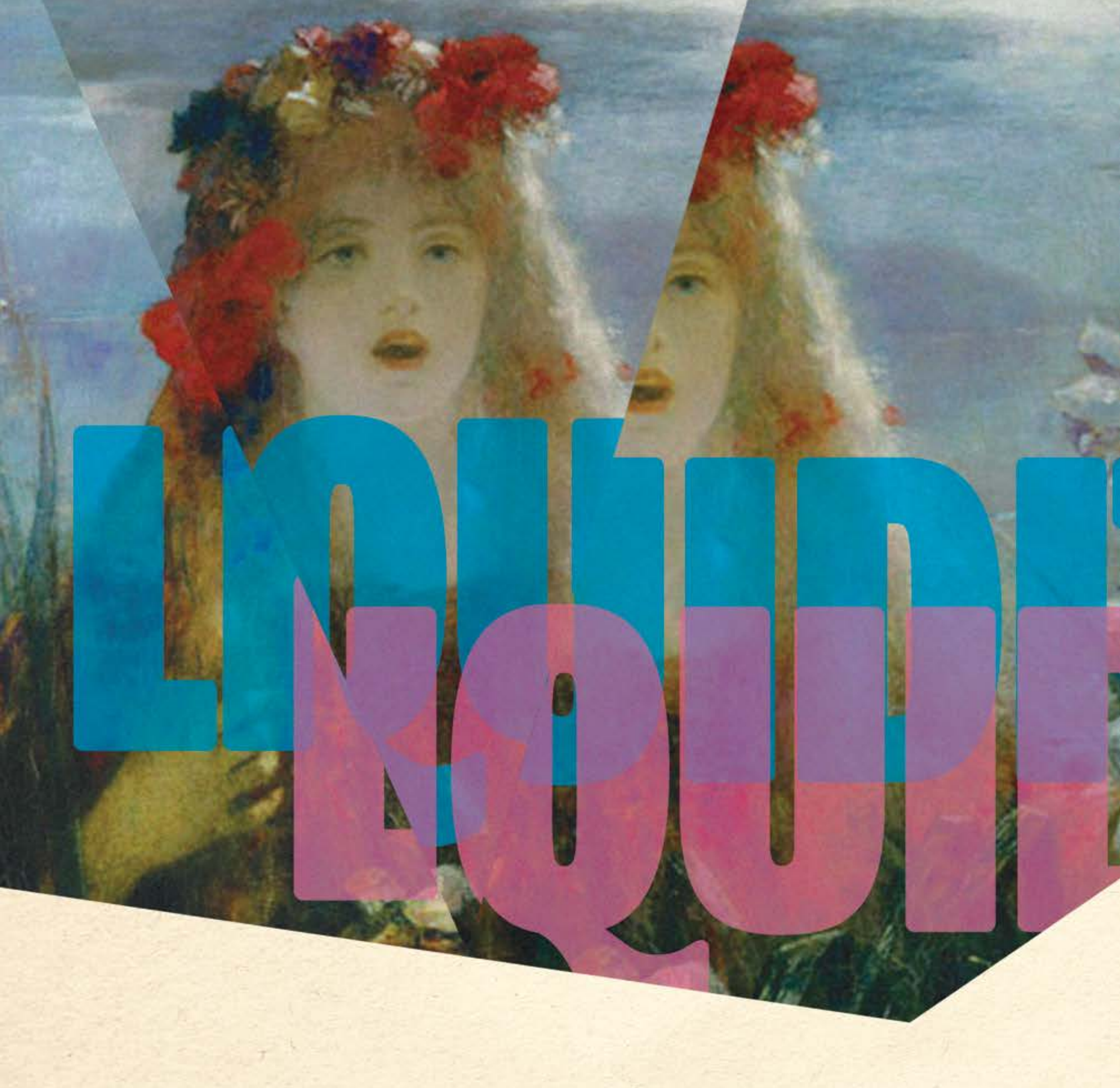
Where did we think this would go as an industry? Over the last five years, the asset class has grown, but it hasn't grown solely as a result of increasing flagship fund size, but also from a proliferation of funds, like mushrooms run wild in the dark fields. A large buyout fund, then a buyout fund for smaller companies, then a buyout fund for companies we'll hold forever, then a buyout fund for companies we can't fit anywhere else, then a credit fund to fund everyone else's buyouts that outbid us.... It goes on and on, with no regard to the real supply of capital out there.

No, this is not a problem of needing more limited partner capital; this is a problem of insatiable general partner demand for money that doesn't exist. And, to add pressure to this situation, for the first time, large parts of the industry have sold major pieces of themselves to companies that only care about one thing: Grow, grow, grow, so that our 25% share throws off oodles of cash to pay our own limited partners and some paper capital gains to boot. In any other industry, there would be a shakeout and consolidation and wailing and gnashing of the teeth. Not in the private markets. The locked-in funds last forever and the option value of a future windfall, however remote, is too great.

No, we are going to live through a multi-year period of more concentrated growth, more challenged fundraises and internal pressures at many shops. Think back on what we saw in the venture industry after the dot-com debacle. Likely not as bad, but still challenging for many. And private wealth? It will serve to concentrate the “winners,” because the barriers to entry are actually quite high and, without scale and brand, it is too hard to play. And so, as we stand here alone on this stage and contemplate moving on to the next part of this overview, we’ll leave you with a few thoughts about private wealth.

- One, increased allocations to private markets from this channel will continue. Why not? It is a return-driven market, and returns are better. Unlike the institutional market, with so many competing political and bureaucratic demands, the private wealth channel is far more focused on what actually matters. The Hamilton Lane 2034 Market Overview will show private wealth investors, on average, allocating 50% of their portfolios to private markets.
- Two, all the innovation in private investing structures and strategies will come from the private wealth side and not the institutional side. In that 2034 overview, institutional investors will be investing like the private wealth side, not the other way around. The demand for information, transparency, data analytics will all be driven by the private wealth side.

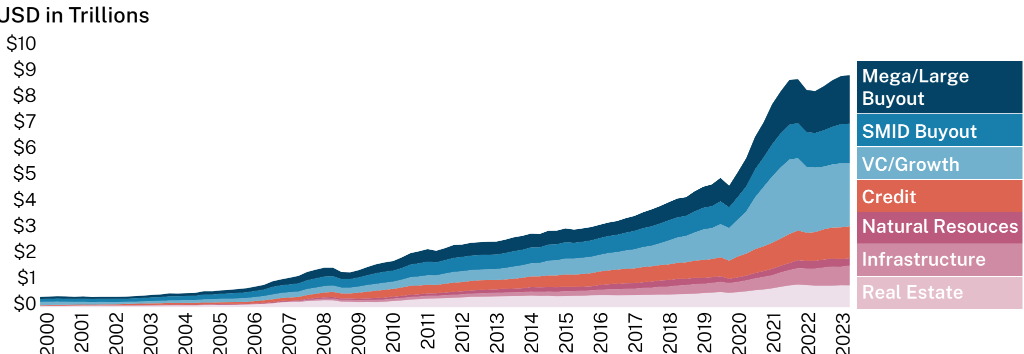
"Unlike the institutional market, the private wealth channel is far more focused on what actually matters.



Liquidity

ast year, we saw the industry's net asset value ("NAV") decline for the first time in years. Where is it now?

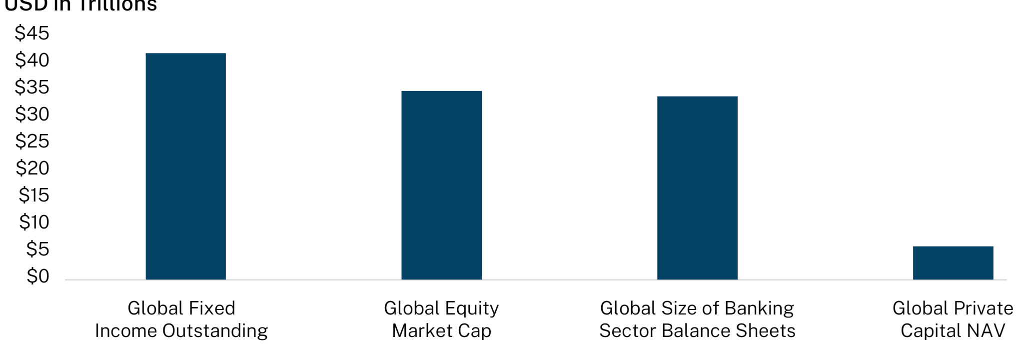
Chart 5.1: NAV by Strategy



Source: Hamilton Lane Data (January 2024)

Who doesn't love a comeback, right? It's interesting that the recent increase is being led by the buyout side of the industry, consistent with our comments earlier about the robustness of earnings in this part of the market. What about the scale of the private markets in general? We'd be hard-pressed to drown out the breathless descriptions of the industry's size in the media and from various pundits bemoaning how the growth threatens to make private markets the largest market on Earth. We are going to borrow another chart from Torsten Slok at Apollo to put some of this in perspective.

Chart 5.2: Growth in Public and Private Markets Since 2013



Source: SIFMA, BIS, Pitchbook, Apollo Chief Economist, Hamilton Lane Data (January 2024)
BIS Data as of 2022 and Q2 2023, Hamilton Lane Data as of Q3 2023

While we in the industry may act as though the private markets are the behemoth of the investing universe, and the asset class has certainly grown over the last 10 years, it's nevertheless grown on an absolute level far, far, far, far less than some more traditional capital sources.

One of the oft-cited reasons for the lack of institutional capital available for fundraising is the lack of money being returned to limited partners to reinvest. What is happening to distributions?

Chart 5.3: Annual Private Markets Distributions

All Private Markets Distributions
All Private Markets Rate of Distribution
USD in Billions
$2,000
$1,800
$1,600
$1,400
$1,200
$1,000
$800
$600
$400
$200
$0
Distributions as a % of NAV
60%
50%
40%
30%
20%
10%
0%
2000
2004
2008
2012
2016
2020
2023
Q1
Q2
Q3
Q4
All PM Average: 24%

Source: Hamilton Lane Data (January 2024)

Across all private markets, distributions are down, although the absolute levels are fairly consistent with what we saw in the years prior to the unusual spikes in 2021 and 2022. It only feels far worse because the NAV has grown so much that the rate of distribution relative to that NAV is down to the levels experienced at the depths of the GFC. We think Janis Joplin sang a song about this feeling...

Across all private markets, distributions are down.

Is this lack of distributions an industry-wide phenomenon?

Chart 5.4: Annual Private Equity and Credit Distributions

Source: Hamilton Lane Data (January 2024)

Oh, did you think credit was going to help you out here? Not so much. There's certainly some distribution from increased interest rate payments, but the bulk of distributions would come from repayment/refinancing. Look at both venture and buyout, which are now at the rates of distribution seen during the GFC. Ouch.

Note to general partners: Please look carefully at these charts. We hear you tell limited partners that you are returning lots of capital. You are… kind of. Stop living in a bubble. You are returning lots of capital, but you have a boatload of capital still locked away. The latter has grown far faster than the former.

Wake up!!!!

The news is a little (emphasis on "a little") better for infrastructure and natural resources distributions.

Chart 5.5: Annual Private Real Assets Distributions

All Private Real Assets Distributions | Real Estate Rate of Distribution | Infrastructure Rate of Distribution | Natural Resources Rate of Distribution

USD in Billions: $0–$450; Distributions as a % of NAV: 0%–60%; 2000–2023; Q1, Q2, Q3, Q4

All PM Average: 24%

Source: Hamilton Lane Data (January 2024)

Wow, look at real estate. Party on like it's 2009, Wayne and Garth!

At the end of the day, for most investors, you want your money back from your private investments before the sun goes supernova and extinguishes life on Earth.

Chart 5.6: Pooled DPI by Vintage Year

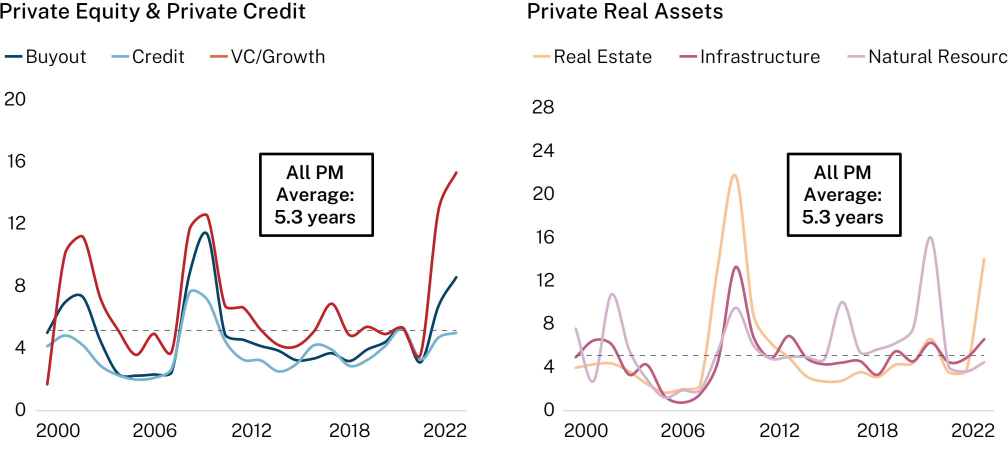
2012	2013	2014	2015	2016	2017	2018	2019	2020
		Late Stage VC 3.9x						
Seed/Early VC 3.5x	Growth Equity 1.9x	Growth Equity 1.8x	Growth Equity 1.3x					
Multi-Stage VC 1.9x	Multi-Stage VC 1.9x	Multi-Stage VC 1.5x	US SMID 1.3x	Seed/Early VC 1.3x	U.S. SMID 0.9x	Infrastructure 0.6x	Mezzanine 0.6x	
Late Stage VC 1.7x	Seed/Early VC 1.7x	U.S. Large/Mega 1.5x	Late Stage VC 1.1x	Growth Equity 1.3x	U.S. Large/Mega 0.8x	EU Buyout 0.6x	Late Stage VC 0.5x	Natural Resources 0.4x
Growth Equity 1.6x	Mezzanine 1.5x	EU Buyout 1.5x	U.S. Large/Mega 1.1x	U.S. SMID 1.1x	Growth Equity 0.8x	Real Estate 0.5x	Natural Resources 0.5x	Distressed Debt 0.3x
U.S. SMID 1.5x	U.S. SMID 1.4x	Seed/Early VC 1.2x	EU Buyout 1.1x	EU Buyout 1.1x	Real Estate 0.8x	U.S. Large/Mega 0.5x	Distressed Debt 0.5x	Mezzanine 0.2x
U.S. Large/Mega 1.5x	EU Buyout 1.4x	ROW 1.2x	Seed/Early VC 1.1x	Real Estate 0.9x	Distressed Debt 0.7x	Distressed Debt 0.5x	Growth Equity 0.4x	Growth Equity 0.2x
EU Buyout 1.5x	U.S. Large/Mega 1.3x	U.S. SMID 1.2x	Real Estate 1.0x	Mezzanine 0.9x	Mezzanine 0.7x	U.S. SMID 0.5x	ROW 0.3x	Real Estate 0.2x
All PM 1.3x	**All PM 1.2x**	**All PM 1.2x**	**All PM 1.0x**	**All PM 0.9x**	**All PM 0.7x**	**All PM 0.5x**	**All PM 0.3x**	**All PM 0.2x**
Infrastructure 1.3x	Distressed Debt 1.1x	Infrastructure 1.1x	Mezzanine 1.0x	U.S. Large/Mega 0.8x	Infrastructure 0.7x	Mezzanine 0.5x	U.S. SMID 0.3x	ROW 0.2x
Mezzanine 1.2x	Real Estate 1.1x	Distressed Debt 1.0x	Infrastructure 1.0x	ROW 0.8x	EU Buyout 0.6x	Late Stage VC 0.4x	Real Estate 0.3x	U.S. SMID 0.1x
Real Estate 1.2x	Infrastructure 1.1x	Real Estate 1.0x	ROW 1.0x	Natural Resources 0.8x	ROW 0.6x	Growth Equity 0.4x	U.S. Large/Mega 0.3x	Infrastructure 0.1x
Distressed Debt 1.2x	ROW 1.0x	Mezzanine 0.9x	Natural Resources 0.9x	Distressed Debt 0.7x	Natural Resources 0.6x	ROW 0.3x	EU Buyout 0.2x	EU Buyout 0.1x
ROW 1.1x	Natural Resources 0.7x	Natural Resources 0.7x	Multi-Stage VC 0.9x	Infrastructure 0.6x	Multi-Stage VC 0.4x	Multi-Stage VC 0.3x	Infrastructure 0.2x	U.S. Large/Mega 0.1x
Natural Resources 0.8x			Distressed Debt 0.8x	Multi-Stage VC 0.4x	Seed/Early VC 0.2x	Natural Resources 0.2x	Seed/Early VC 0.1x	Multi-Stage VC 0.1x
						Seed/Early VC 0.1x	Multi-Stage VC 0.1x	Late Stage VC 0.0x
								Seed/Early VC 0.0x

Source: Hamilton Lane Data (January 2024)

For a time early in the twenty-teens, venture and growth were the kings of returning capital. Alas, much like King Hamlet's, that era is gone. It is interesting to see the credit-oriented strategies assume leadership roles in returning capital, but it is obvious that the entire industry in general is struggling to get money back to investors. Until that changes, we doubt the fundraising environment is going to strengthen. (That was a thinly veiled attempt at subliminal messaging to the GP community…)

Not surprisingly, the average time to liquidate the NAV has shifted dramatically over the last few years.

Chart 5.7: Years to Liquidate NAV



Source: Hamilton Lane Data (January 2024)

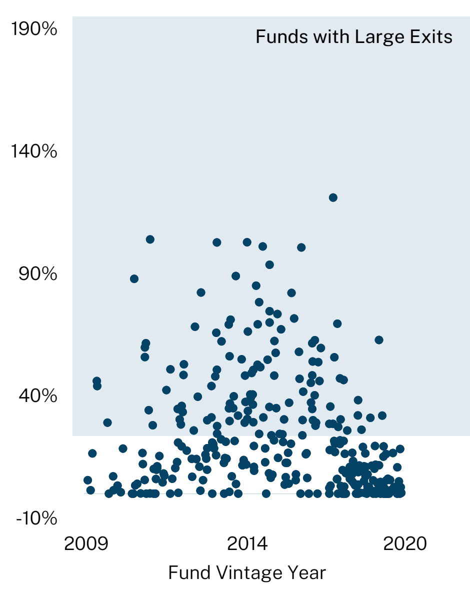
Look how far above average are buyout, venture and growth and real estate currently. What will change that? Ironically, when there were previously peak periods similar to what we see today they were wonderful buying opportunities. Will that history repeat itself?

Let's wander back to our charts that plot the star distribution in the Milky Way and see what clues they offer about what age funds distributions were coming from.

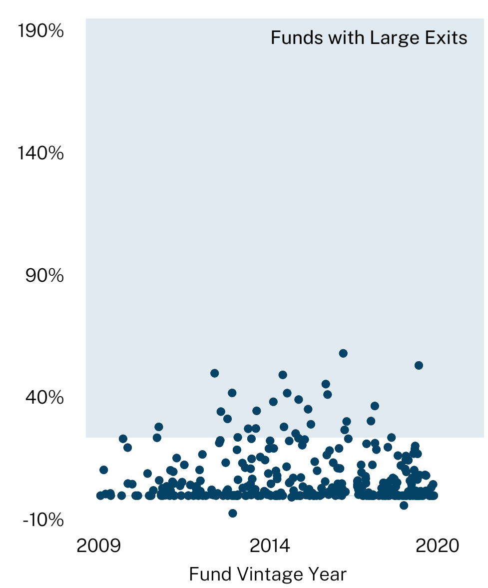
It is obvious that the entire industry in general is struggling to get money back to investors.

Chart 5.8: Distributions as % of Fund Size by Fund

Calendar Year 2021



Calendar Year 2023



Source: Hamilton Lane Data via Cobalt (January 2024)

In Chart 5.8, we are comparing individual distributions in 2021 and 2023. You can see that in 2021, young and old funds alike were selling companies, with some hefty amounts (relative to the size of the respective funds) coming back from individual sales. Perhaps surprisingly, many of those were coming from younger funds. In 2023, the number is down significantly across all age groups.

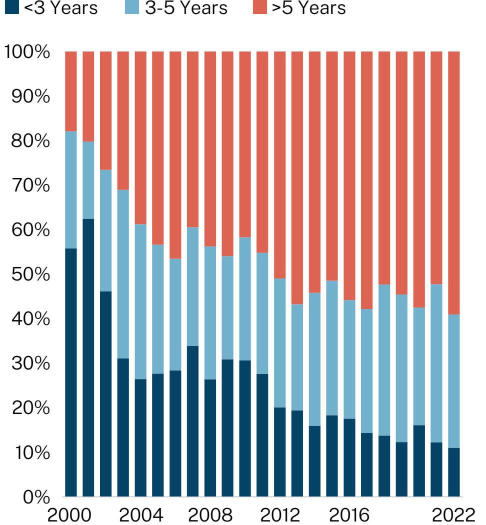
There are a few important things investors need to understand from these charts. First, there is a notion that this is an industry where funds send back some relatively smooth amount of capital every year because they are selling a relatively consistent number of companies. Nope. This is an industry where distributions tend to be very large — coming from a small number of portfolio companies—or very small. It's lumpy. 2021 was very large, 2023 was small. That's not a bad thing per se, but it means you have to pay attention (again) to portfolio construction. Too much concentration, whether in funds or co-investments, will have a bearing on that distribution profile. We are not saying that the funds' values are concentrated in a small number of companies, but that their distribution profile usually is.

Holding periods are, unsurprisingly, getting longer.

Chart 5.9: Holding Periods

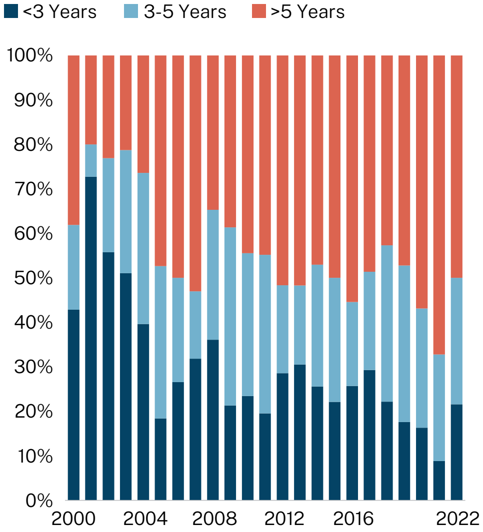
Holding Period of Exited Buyout Deals

% of Deal Count by Year of Exit



Holding Period of Exited Growth Equity Deals

% of Deal Count by Year of Exit



Source: Hamilton Lane Data (January 2024)

We'll be "Masters of the Obvious": Longer holding periods will lead to reduced IRRs, all else being equal.

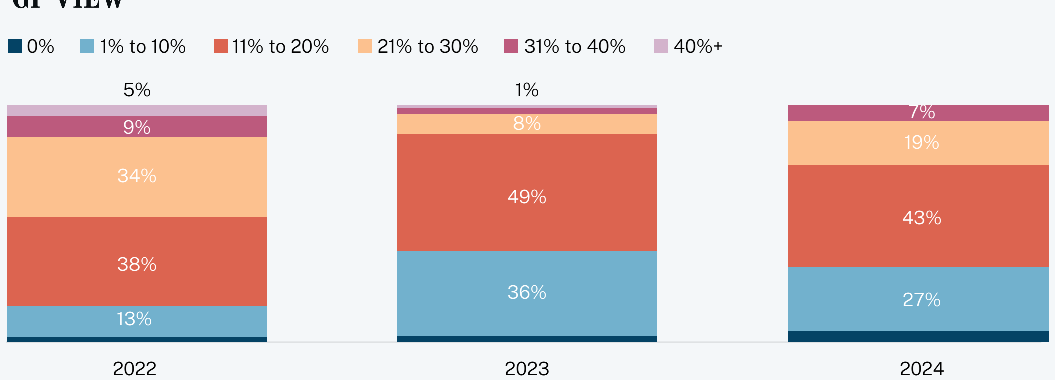
Yes, that's us…

But what do general partners think of the exit environment coming up?

GP VIEW

Chart 5.10: GP Survey – Exit Options

What % of your current portfolio is actively pursuing an exit process with expected closings in the next 12 months?



Source: Hamilton Lane General Partner Survey 2023 - 2024 (December 2023)

GPs see an increase in the intended exit activity. While we often offer that they are an optimistic group, we note that they were correct last year that we would see a decline in exit activity so, for those investors hoping for more money back from their private portfolio, this is a good sign.

Another interesting datapoint coming out of our survey concerns IPO activity. There is a fairly common belief that exit activity is tied to IPO activity. What is the percentage of exits that are expected to happen through the IPO channel? The number you would expect based on what you hear people believe is something like 25%. The actual number reported by our surveyed GPs suggests that only 4% view IPOs as the most attractive exit option. You read that correctly. The reality is that, outside of some venture firms, IPO activity is not a real path to exits for the private markets industry. IPO activity matters because high levels generally mean confident capital markets, but the IPO road is one less traveled for the private world.

{A Brief Pause for a NAV Loan Primer}

"Though this be madness, yet there is method in it."

We bid you step away from the soap box, because it's our turn to stand on it.

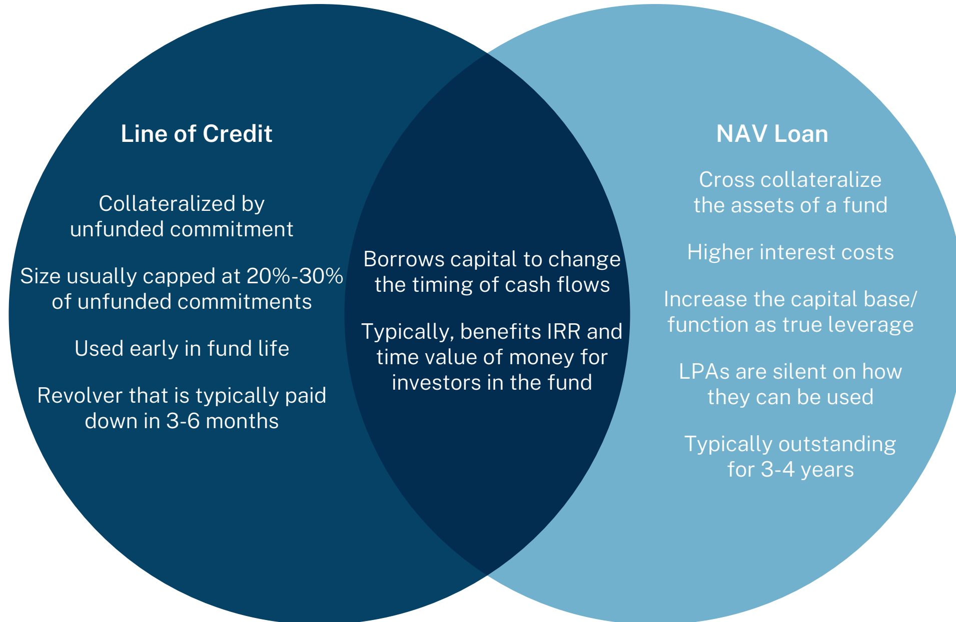
What happens when you take an industry that is looking for exits (yes, both LPs and GPs want the same thing on that account!), has a desire to lock in IRR in the face of an uncertain future, lacks easy access to additional limited partner capital, and contains a bunch of people who spend a lot of time doodling with financial engineering?

You get the NAV loan. What is a NAV loan, other than the number one topic at any limited partner meeting? The concept is easy enough: I will lend you, the general partner, some amount of money at the fund level and I will receive, as collateral, your interest in your portfolio companies. You can do whatever you want with that money. You can use it to lend to a company in your portfolio or you can send it back to your limited partners.

A big part of the conversation is being driven by the growing number of providers who are eager to structure these loans with GPs and LPs. While these groups come in many shapes and sizes with varying levels of expertise, one nearly universal theme in their pitch is to compare NAV loans to lines of credit. What we can't always tell is whether they believe in the similarities or if, instead, they hope the market for NAV loans grows in a similar way...

Based on the fees they earn for these loans, we could take a guess.

While there are certainly some similarities, we respectfully disagree with the broader premise and would argue that NAV loans have a different impact from both a risk and cost perspective. While by no means an exhaustive list, we jotted down a few ideas.



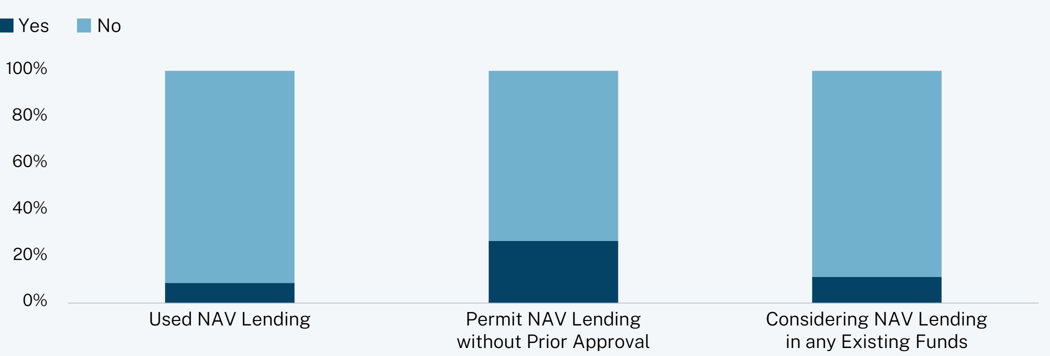
When we consider the differences, our immediate reaction is that any GP asking to use a NAV loan has a performance issue – either at an individual company, with their IRR compared to peers, or with an underwhelming DPI. How they propose to use the NAV loan will give you fairly good insight into where that issue might be.

And just how prevalent is this practice? Surprisingly, given the discussion about it, not as widespread as you might imagine.

When we consider the differences, our immediate reaction is that any GP asking to use a NAV loan has a performance issue.

Chart 5.11: GP Survey – NAV-Based Lending

GP Use of NAV Loans



Source: Hamilton Lane General Partner Survey 2023 - 2024 (December 2023)

We're probably dealing with around 15% of managers. This number could be much higher as managers are organized to be able to engage in this lending activity. Interestingly, the trend is led by Europe, both in terms of total number of GPs using it and also when the theme was first starting to become popularized. We would remind you that this is the exact opposite geographic trend we saw play out during the advent of credit line usage. Europe was much slower to adjust to lines of credit when compared to North American GPs. While we're not certain why this is the case, we find the deal-by-deal – excuse us, region-by-region – difference quite fascinating.

What is really obnoxious is that more than 20% of agreements allow the use of this borrowing without prior limited partner approval. That is ridiculous. LPs, now it's your turn to wake up! Don't allow this without your approval. Full stop.

What is the net impact of a NAV loan? Obviously, it will depend on the specific terms, but we made some assumptions. Ok, you borrow 20% of the fund size, you pay 11%. (Why 11? Why, because it's our homage to "Spinal Tap" of course! Oh, and because it's also what we understand to be in the middle of the range of current market rates.)

What do you get? A gross return of 25%. Voila.

Chart 5.12: Impact of NAV Lending

Impact from Using a NAV Line		
Assumes 25% Gross IRR, 20% LTV, 11% Coupon		
	Proceeds Fully Distributed	**Proceeds Recycled**
Impact on Net IRR	0.98%	0.73%
Impact on TVPI	-0.08x	0.20x

If you send the money back to limited partners, your IRR goes up by a hundred basis points, but your distributed capital goes down over the fund life. If you use the money to invest in a portfolio company, your IRR only increases by 75 basis points, but your multiple goes up by 0.20x. We see why this is appealing to general partners. It does two things: It helps lock down a higher IRR and it helps reduce the time needed to generate carry by returning capital and reducing the time that pesky preferred return is running.

Now look at what happens if returns aren't as rosy as hoped. Use the same 20% of fund size at 11%, but now the fund returns decrease to 10% after you borrow the money.

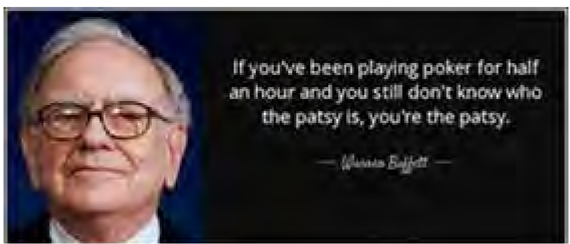
Impact from Using a NAV Line		
Assumes 25% Gross IRR, Decreasing to 10% at outset of NAV Line, 20% LTV, 11% Coupon		
	Proceeds Fully Distributed	**Proceeds Recycled**
Impact on Net IRR	0.36%	-0.46%
Impact on TVPI	-0.08	0.01x

Now, your IRR only increased by 36 basis points, and you reduced the same multiple of capital. If you recycle the money, your IRR goes down by 46 basis points (you are paying more interest than you are earning on your investment), and your multiple is basically the same. We were also surprised at the relatively minor impact on IRR in the distributed scenario, but it tells you the power of locking in the IRR early. Sometimes, the trickster is rewarded. (It's also a function of us being fair and using the three-year point. Those numbers change quite a bit depending on your amounts outstanding and where in the fund's life this is happening – the later it is, the lower and the less favorable these comparisons will look).

So why do we hate these types of loans? Let us count the ways.

- LPs did not enter into the commitment with the idea that their investments would be cross-collateralized. LPs are ok with leverage on individual companies and don't worry that too much leverage on one will impact the value of another portfolio company. Each company stands alone. Cross collateralizing, particularly without consent, is dumb.
- While LPs want money back, think about the economics. The LP is, through the GP, borrowing money at 11% to pay itself back. Most LPs have a lower cost of capital than that and don't need GPs to borrow for them. It's a terrible capital allocation decision.

- This structure is so GP-favorable that it requires a conflict of interest vote from advisory boards. It so favors the GP by locking in an IRR and cutting off the running of the preferred return clock that LPs should have a say in its use. Moreover, if the capital is going to be used for a portfolio company, why can't that portfolio company borrow these funds at that rate? We aren't talking concessionary rates here.
- All you need to know here is that lenders are salivating at these kinds of loans. They are high yielding and massively over-collateralized. It's the limited partners paying the yield and it's their assets that are being collateralized.



The lost (and now found) fragment of Hamlet's Act 3, Scene 1
Much is known about Shakespeare, while much remains shrouded in mystery. "Hamlet," for example, represents a compilation of numerous versions and sections found over the years without any certainty of when it was written or what that original version contained. Enough is known about Shakespeare himself, however, to know that he was regarded as a shrewd businessperson and investor. In fact, one note about his investment style is that he routinely made major investments every three years. It's been said that was because he was conservative and liquidated one investment to make another. Of course, we in the private markets business have already figured out what you instantly understood upon reading that sentence: Shakespeare was one of the first private markets investors in history and divined the three-year investment period!

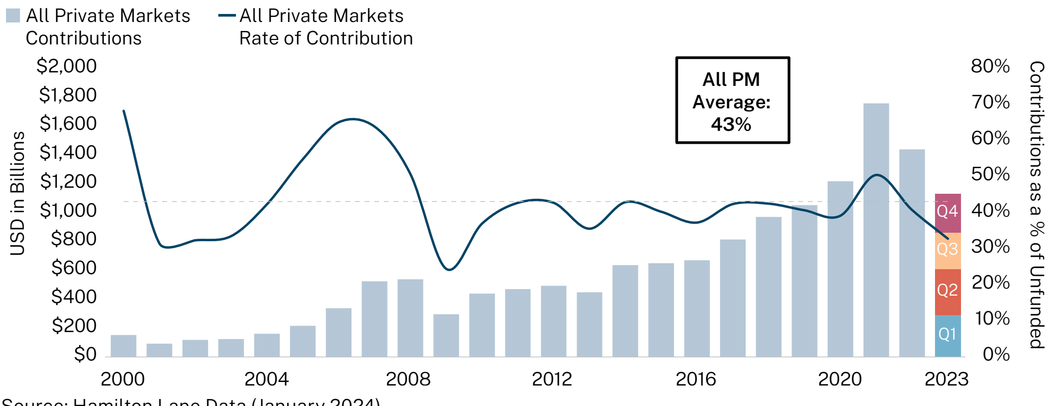
It is with that background that we are excited to introduce, for the first time, further evidence of Shakespeare's private markets roots. In the course of our research for this market overview, we spent time in his ancestral home in Stratford. As you know, no manuscript of Shakespeare's works exists, since paper, even with someone's play written on it, was used for scrap, for baking dishes or for wrapping odds and ends. We found, buried deep in the attic of that home, old candlesticks swaddled in ancient and cracking paper. On one we found, and have deciphered, what we were amazed to see is likely an early draft of Hamlet's famous "to be or not to be" soliloquy. Tell us this doesn't speak to the world of private investing! Why, oh why did Shakespeare change the meaning from these profound words you are about to read to the hardly memorable musings of a nearly forgotten and terribly cranky noble? We shall never know. But think how famous Shakespeare could have been had he stayed to his own self true and kept Hamlet as the Prince of Private Equity!

To invest, or not to invest: that is the question:
Whether ‘tis better to hoard my cash and suffer
The slings and arrows of those who want their money back,
Or to invest — invest in what? Credit, infra, real estate, buyout, VC?
To invest and bear the uncertainty of where,
Of where we shall our next farthing find?
When investors all around make mockery,
Grinning leers with pockets empty.
‘Tis an uncertainty to make minds bend,
And find solace in silence and inaction?
And to invest to say we end the doubt and the
Thousand natural shocks that our indecision is heir to,
‘Tis a consummation devoutly to be wished.
To invest, make more, more money:
Perchance create a huge IRR; ay, there’s the rub:
For in that investment what disasters may come?
When we have realized our dismal choice,
Must give us pause.
For who would bear the whips and scorn of second guessers?
The insolence of other investors who boast of better returns?
That dread of something after we invest
And makes us rather bear the indecision we have,
Than fly to others that we know not of?
One poor investment thought doth make cowards of us all!

Investment Activity

et's not kid ourselves and think it's only the limited partners who have been wringing their hands and playing the part of Hamlet, adrift in indecision—where to invest, how to commit —preferring to do little.

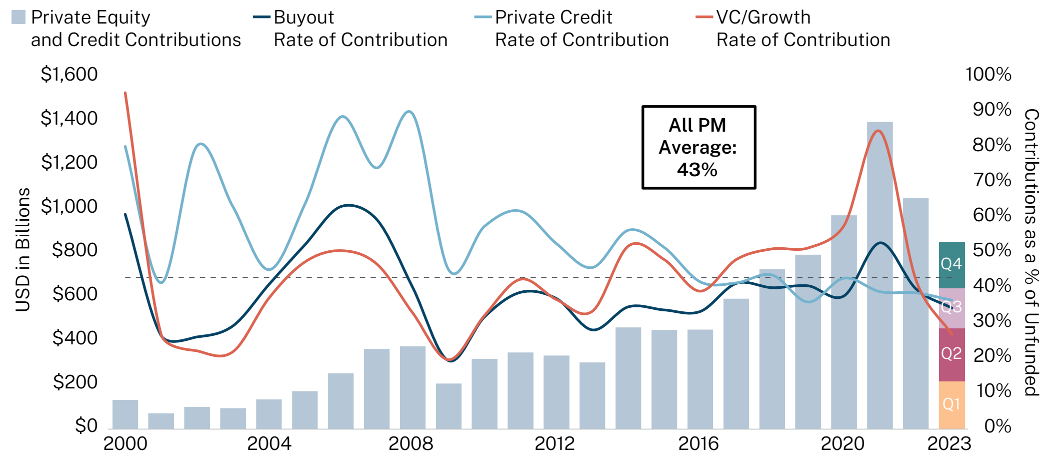
Chart 6.1: Annual Private Markets Contributions



Source: Hamilton Lane Data (January 2024)

Despite the bravado, general partners are also sitting on their hands. Investment activity as a percentage of unfunded capital is at levels seen during the depths of the GFC. As with distribution activity, it might seem like it's active on an absolute level, but that is not the case when you consider the growth in the industry. This relative lack of activity holds true across most parts of the industry.

Chart 6.2: Annual Private Equity and Credit Contributions



Source: Hamilton Lane Data (January 2024)

It is surprising, given the high level of interest rates, to see credit activity so light, but that is likely a function of the reduced deal activity. On the real assets side, the story isn't all that different.

Chart 6.3: Annual Private Real Assets Contributions

All Private Real Assets Contributions
Real Estate Rate of Contribution
Infrastructure Rate of Contribution
Natural Resources Rate of Contribution

USD in Billions: $0, $50, $100, $150, $200, $250, $300, $350, $400, $450

Contributions as a % of Unfunded: 0%, 10%, 20%, 30%, 40%, 50%, 60%, 70%, 80%, 90%

All PM Average: 43%

Q1, Q2, Q3, Q4

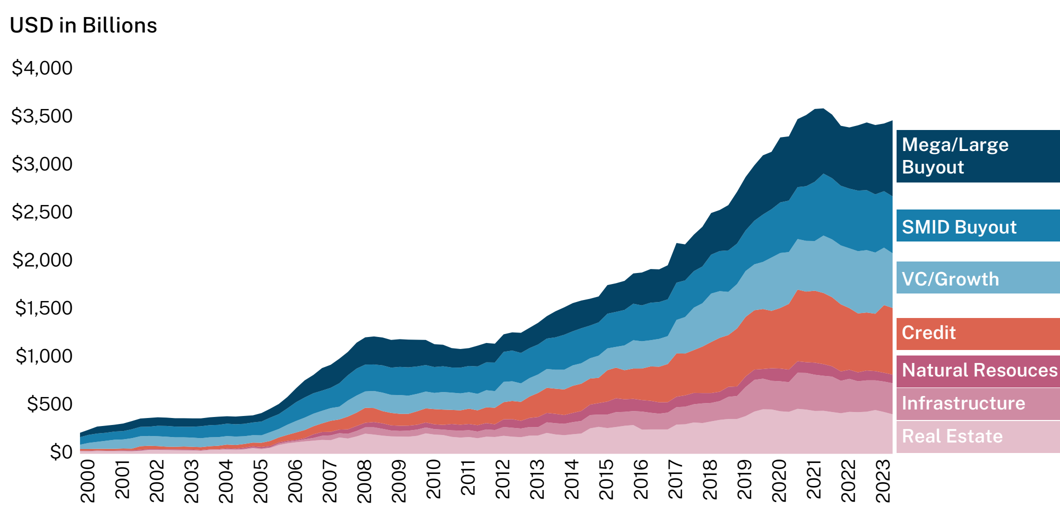
2000, 2004, 2008, 2012, 2016, 2020, 2023

Source: Hamilton Lane Data (January 2024)

Again, look at those real estate numbers. We are at a similar level of deal activity as we saw during the GFC.

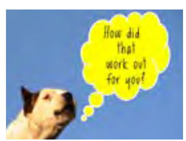
This brings us to the chart we love to hate. There may be some debate on the most important chart in this overview, but little doubt on the least important. Ladies and gentlemen, for your consideration...

Chart 6.4: Capital Overhang



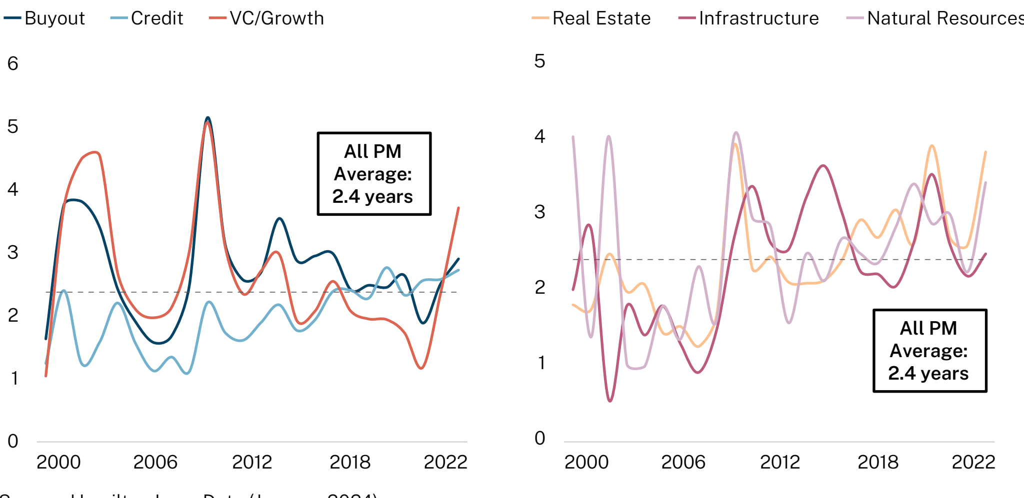
Source: Hamilton Lane Data (January 2024)

Truthfully, we don't hear as much talk about the capital overhang as we did a few years ago. Perhaps because it has gone down somewhat over the last couple of years. Out of sight; out of mind. But we have yet to see any kind of correlation between the amount of overhang and the level of returns. We have told this story, but will tell it again because it is so dramatic an example of reality being so different from appearances. We were told by the CIO of a very prominent fund in 2008 or 2009 (at our age, we are lucky if we remember the decade something was said to us) that he was halting all private investments. Why? Look at that chart and the huge run up in dry powder from 2005 to 2008. He had determined that it could only mean one thing: Lower returns.



This next chart, on the other hand, we respect, on the other hand, we respect more and more each year.

Chart 6.5: Time to Deploy Capital Overhang



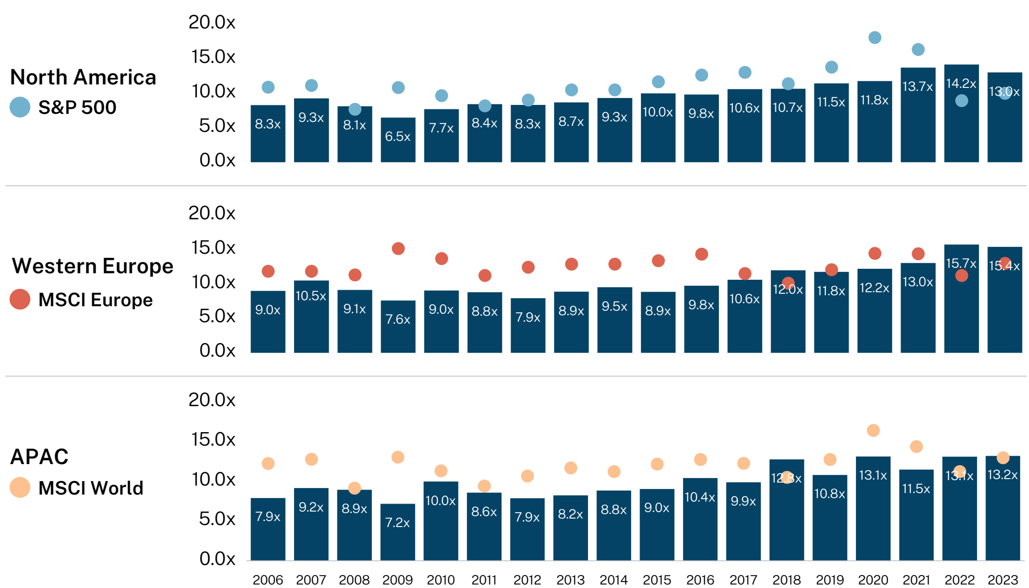
Source: Hamilton Lane Data (January 2024)

This essentially measures the speed at which money is being spent. When we see some segment of the market hit peaks or troughs, it sets our radar on alert that the market is entering an interesting buy or sell period. (We know, we are a long-only asset group, so we aren't selling but we are slowing down our buying.) Note that the VC/growth side of the market gave out that signal in 2020/2021, which proved very prescient. Buyout did the same in 2007 and came pretty close in 2021. Right now, the indicators are all suggesting that we are closer to good buying territory, similar to what we saw in 2003 and 2009. It is interesting that the real assets side of the investment world has much more volatility, making it harder to read signals from that area.

Let's turn to what, if we took a vote among the ten people who read this market overview in its entirety, would be selected as the most important chart in the book.

Chart 6.6: Purchase Price Multiples at Acquisition

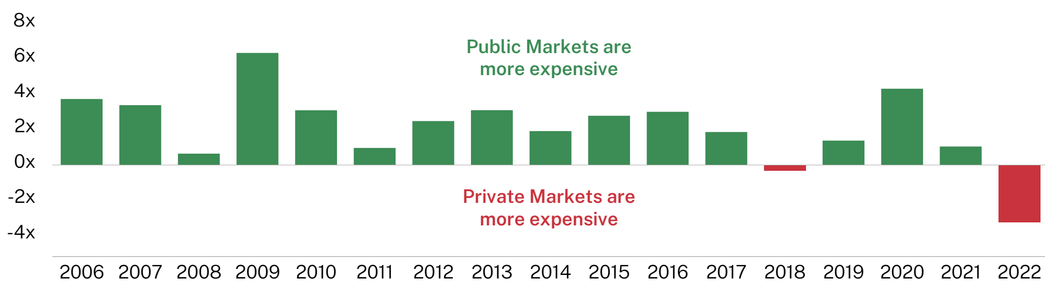
Median EV/EBITDA by Deal Year



Source: Hamilton Lane Data, Bloomberg (January 2024)

Investors are fixated on purchase price multiples. This chart is trotted out at bars, cocktail parties, libraries, and bowling alleys and discussed as to what it means for returns and life in general. We are not oblivious to the importance of purchase prices. If you pay too much, it's hard to make any kind of return. Ah, but what is too much? That is a vexing question. Right now, multiples in the private markets are at record levels in Europe and Asia and close to that in the U.S. More importantly, they are now higher than what is found in the public markets. How rare is that occurrence?

Chart 6.7: MSCI World Buyout Deal Purchase Price Spread



Source: Hamilton Lane Data, Bloomberg (January 2024)

Really, super-duper rare, particularly by the degree to which it is now. The time it happened in 2018 was actually a decent time to buy, but we are in new territory, and this is a very common reason investors are citing to avoid private equity investing. Perhaps. (We will discuss that in somewhat more detail later). Right now, we are going to give a pure anecdote in an overview otherwise filled with data and facts. It's one of our favorite stories.

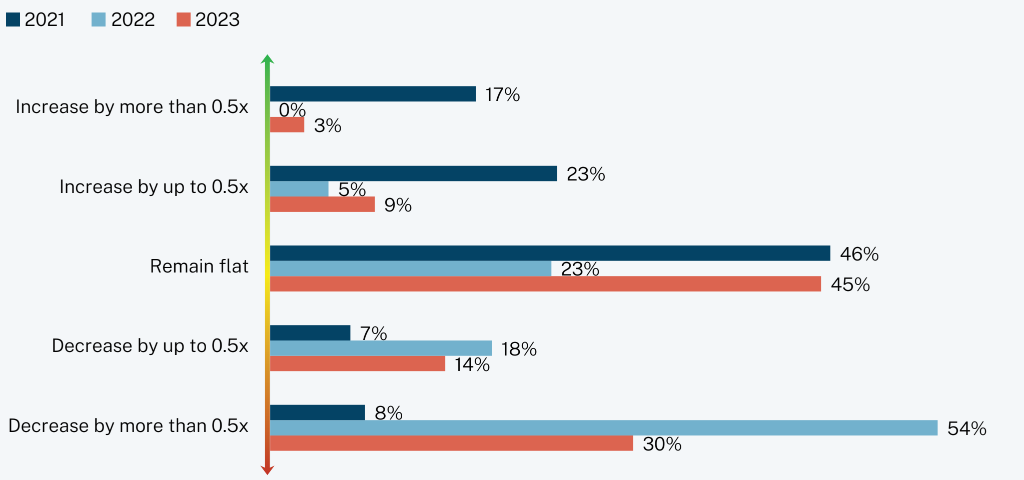
Ted Forstmann was one of the great early investors in the private equity world.

Think of Gulfstream, IMG, Yankee Candle, Dr. Pepper (ok, so he made some lousy ones too). An interesting tidbit is that he coined the term "barbarians at the gate." Though Ted died in 2011, we bring him up because he said something to us long ago that has always stuck with us. He said, roughly quoted, "Of the ten most important things in a successful buyout, price is number 11."

Indeed, there is nothing either good or bad but thinking makes it so…

Ok, general partners, your turn to tell us where prices are going.

Chart 6.8: GP Survey - Purchase price multiples (EV/EBITDA) over the next 12 months will:



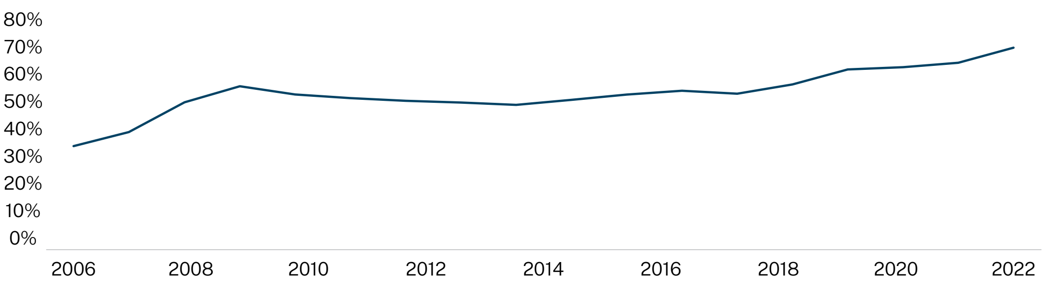
Source: Hamilton Lane General Partner Survey 2023–2024

They expect prices to remain flat or decrease in the next 12 months. This is one place where we are dubious about their seer status. They were looking for higher prices in 2021 going into 2022 and that was clearly wrong. We have found this particular prediction model to be far more of a trend following model than other places where we get general partner input.

One reason we have been sanguine on both the increase in purchase price multiples and the impact of higher rates on portfolio company operations is Chart 6.9 and what it means.

Chart 6.9: Buyout Deals % Equity Contributed

Median by Deal Year



Source: Hamilton Lane Data (January 2024)

This, dear readers, is the most important chart in this overview. Why? Because it tells you why we are unlikely to see a repeat of the 2002 or 2007 era of buyout returns. The amount of equity that is being invested into deals is higher than it's ever been. That doesn't mean that returns are going to be great. Though they might be, who knows? What it means is that there is so much more equity cushion in deals that the downside risk of loss is diminished. This means more safety for your credit exposure, greater likelihood of general partners supporting companies given their equity levels, and generally fewer wipeouts in portfolios.

Once again, empty the stage and leave the sole figure of Hamilton Lane, now the background music is John Lennon's "God."

Is it time for us to get nerdy and serious? Is that like being cruel to be kind? Because we have spent a lot of time on this question of purchase multiples, both absolute and relative to the public markets. We have spent a lot of time listening to the arguments that we should be watching them closely and making investment judgments based on how high or how low they are relative to prior levels and public levels. We wring our hands, we ponder, we pace, we gesticulate, we sit in our office and wonder what it all means. Then we see this chart.

Chart 6.10: Public vs. Private Multiples Pricing

Median U.S. Buyout ACQ EV/EBITDA Minus S&P 500 EV/EBITDA

Sector/Year	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Industrials	-2.3x	-0.3x	-0.2x	-3.8x	-1.8x	-1.0x	-2.0x	-2.6x	-3.1x	-3.2x	-2.2x	-2.8x	-2.7x	-2.9x	-5.3x	-2.9x	-0.8x	-4.8x
Consumer Discretionary	-3.9x	-1.0x	2.1x	-4.4x	-2.5x	-1.4x	-2.9x	-3.5x	-4.0x	-2.0x	-3.9x	-4.0x	-3.3x	-3.4x	-6.3x	-1.2x	-1.5x	3.9x
Information Technology	-0.8x	0.8x	3.9x	0.1x	-0.4x	-0.2x	0.3x	-0.5x	2.2x	0.4x	0.6x	-2.0x	-0.4x	2.3x	0.1x	7.2x	4.4x	1.9x
Health Care	-3.4x	0.5x	2.7x	-3.1x	-2.4x	0.2x	-2.5x	-5.3x	-5.1x	-2.8x	-3.2x	-3.3x	-1.8x	-2.8x	-4.5x	-2.3x	0.5x	1.7x
Financials	-3.0x	1.5x	-3.3x	-7.4x	-3.8x	-5.3x	-2.3x	-4.5x	-4.8x	-3.6x	-6.0x	-2.1x	-7.0x	-4.4x	-1.6x	-1.7x	3.0x	-1.2x
Consumer Staples	-0.1x	-3.0x	-2.5x	-1.9x	-2.3x	-0.9x	-4.9x	-6.9x	-4.1x	-5.3x	-6.5x	-4.3x	-2.4x	-5.6x	-11.2x	-6.2x	-4.2x	-5.6x
Communication Services	-2.4x	-1.1x	4.9x	-3.1x	0.8x	0.0x	-0.7x	0.8x	-0.7x	-1.6x	-0.6x	-1.7x	1.2x	-0.5x	-0.1x	5.2x	5.1x	-0.9x
Materials	-2.7x	1.1x	-0.1x	-3.4x	-4.9x	1.0x	-3.2x	-3.0x	-3.3x	-5.2x	-6.8x	-5.0x	-0.5x	-4.2x	-5.1x	0.3x	-1.5x	-1.7x

Source: Hamilton Lane Data, Bloomberg (December 2023)

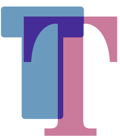
We know this looks too busy and we hesitate even to show it to anyone, but we are convinced it is the most important chart in the overview. What does it say? What bolt from the blue did it create? Those blue shadings tell us that the private markets are buying at a premium to the public world, but now we are looking at different industries, and not at aggregate numbers. Speak to us chart; tell us what you want to say! It seems so obvious, but so outlandish, even to us. Here is what we believe: Yes, private assets are selling for more than public assets today, just as they were in 2007 and 2008, but very focused in certain industries and generally avoiding some. Private never buys at higher prices than publics in industrials and consumer staples. Why? What do they know that the public doesn't? But look at how private buys at higher prices today and during the GFC in healthcare and information technology and even in consumer discretionary. Again, why? Now look at how private equity has consistently bought at a premium to the public markets for the last 15 years in information technology.

Here's why.

No one dares say it aloud in good company, but private equity simply is smarter, better and faster than public equity. The tell is that blue band across time for information technology. Private markets realized very early that infotech was where growth and returns were concentrated and were willing to pay more for it than the public markets. Not because they had to but because they saw what the public markets didn't. The same is true for certain periods when public markets' emotions cause prices to move too dramatically in one direction or the other. Blue concentration in 2007/2008 and 2022/2023 is private markets saying, "Public markets aren't correctly pricing assets for their prospects over the next few years so we will buy them regardless of the premium." This isn't just one general partner, but the aggregate wisdom of the crowd of them and history suggests that they are always correct because the returns have always been superior.

It sounds so arrogant, but there is a reason that these multiples paid swings above and below public market prices occur consistently at certain market turns and consistently around certain market sectors and assets. This isn't dumb luck or random noise.

Secondaries: An Investment for All Seasons



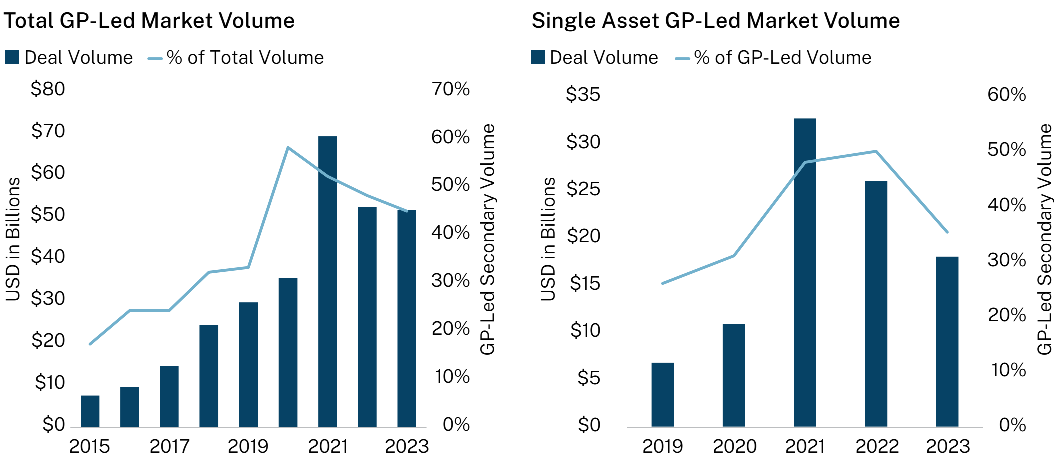
he secondary market is the home of three popular views today.

- You only invest in secondaries to mitigate the J-curve and get access to prior vintage years.
- GP-led secondaries are terrible, because GPs are selling their crappy assets.
- GP-led secondaries, particularly single-asset deals, are just like co-investments.

We'll just note that the first can't be true if the second and third are even remotely true, but nevertheless let's use this section to dig into GP-led secondaries a little more and bring some reality into the discussion.

There is no question that the growth of GP-led secondaries is one of the biggest changes to the private markets landscape in the last five years.

Chart 7.1: GP-Led Secondary Market Growth



Source: Jefferies Global Secondary Market Overview, Evercore 2023 Secondary Market Overview (January 2024)

GP-led transactions have become a major part of secondary deal volume, in some years exceeding the number of LP deals. Remember these didn't even exist eight years ago! Within the GP-led space, single asset transactions have also become a larger component of that sub-market. The reasons are fairly obvious: a desire to sell assets and give LPs money back; GPs wanting to retain some of those assets for a longer period; the economics for both GPs and for placement groups is lucrative.

There's a great deal of chatter about the GP-led space, ranging from "these are wonderful deals" to "these are the worst deals in the history of private equity." Let's try to get some data to help us figure out what's really happening.

Chart 7.2a: GP-Led Continuation Vehicle Performance

By Year of Investment

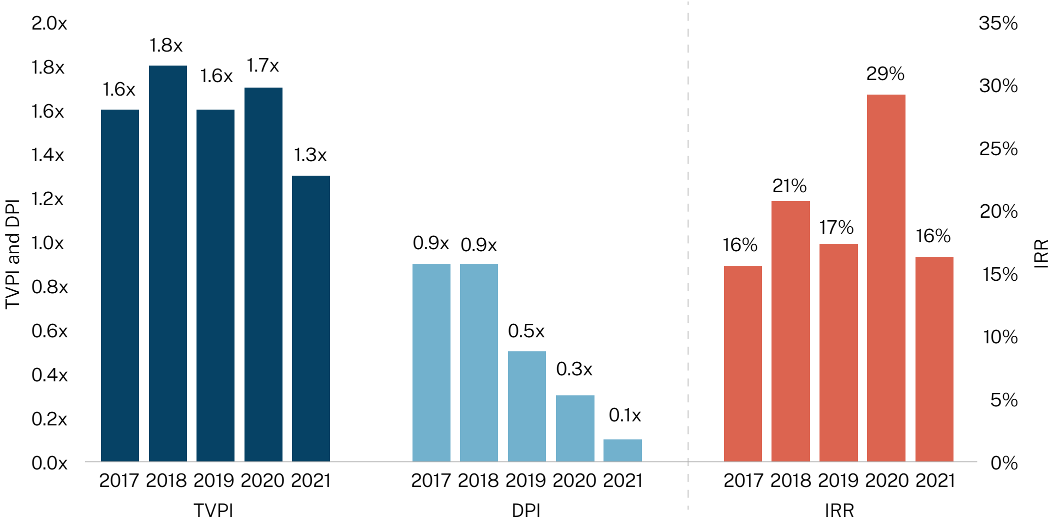
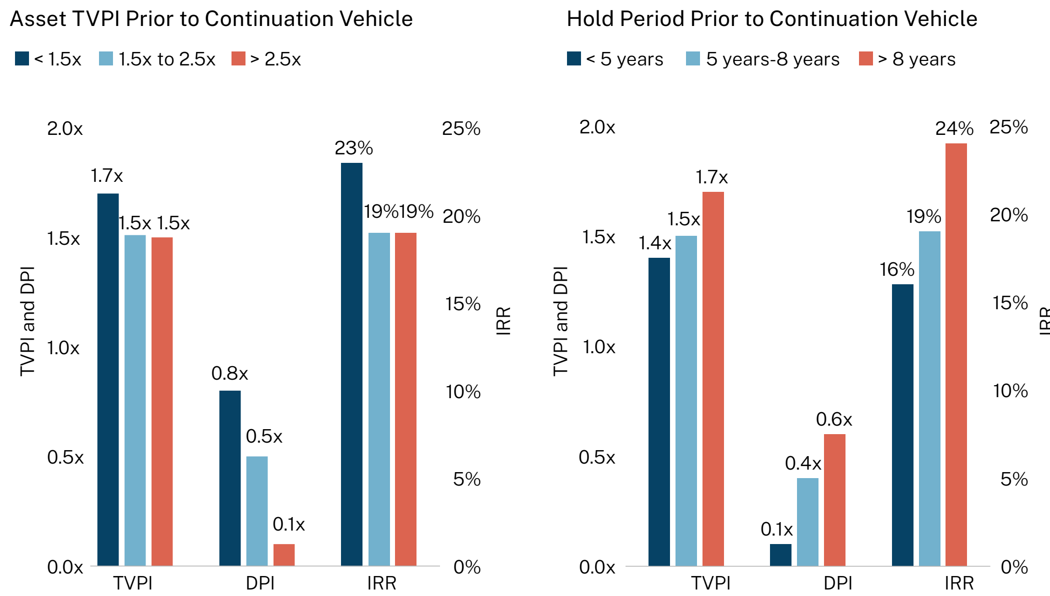


Chart 7.2b: GP-Led Performance by Asset Performance Prior to Continuation Vehicle

Asset(s) Performance Prior to Continuation Vehicle



Source: Hamilton Lane Data (January 2024)

The returns look good, although it's early for most of these transactions. We'd also note that, from a return perspective, these transactions don't seem to have any return premium to LP transactions. Should they? Perhaps given the greater concentration, they should. Can we draw any conclusions about these GP-led deals based on the characteristics of the fund from which they were sold?

{Just an editorial comment here. You have to give us some props for the information you're seeing here. Do you get this stuff anywhere else? We didn't think so…}

We would have said, and bet you would have also said, that better deals are associated with higher prior fund multiple on invested capital and shorter holding periods – the theory being there's more upside with the shorter hold in the fund. The opposite is what early returns suggest. You want to lean into a fund that has lower prior performance and that has been held longer.

The argument we hear all the time is that single asset, GP-led deals are the same as co-investments. Presumably, this means having them benchmarked as co-investments, having different teams work on them if you are structured that way and looking at them with a generally different lens than you do secondaries. Some of that is philosophical and a question of how you organize your team, but are there return profiles that suggest they are the same or different?

Chart 7.3: "Co-Investment" vs. Single Asset Continuation Vehicles

TVPI

Buyout Deals Single Assets Illustrative Single Asset Gross Returns

2.5x 2.0x 1.5x 1.0x 0.5x 0.0x

2018 2019 2020 2021 Average

IRR

Buyout Deals Single Assets

45% 40% 35% 30% 25% 20% 15% 10% 5% 0%

2018 2019 2020 2021 Average

Distribution by MOIC

<0.5x 0.5x –1.0x 1.0x –1.5x 1.5x – 2.5x >2.5x

100% 80% 60% 40% 20% 0%

Buyout Single Asset Buyout Single Asset Buyout Single Asset Buyout Single Asset

2018 2019 2020 2021

Source: Hamilton Lane Data (January 2024)

From a pure IRR perspective and using the buyout index as a proxy for co-investments, buyout deals have outperformed single asset, GP-led deals. Even if you take out fees from those buyout numbers, you would have somewhat outperformed single asset deals. You can see that in Chart 7.3, which exhibits TVPI comparisons. The differences in return are marginal between the two categories. What does appear quite different is the risk profile of the two. The bucketed MOIC bars show that single asset deals have had a much tighter return band and lower loss ratios.

What's our conclusion on these single asset deals, particularly versus co-investments? We don't believe they are the same. To start, these are not lousy assets as the market feared. These are assets that general partners want to keep. This means they are probably safer, lower-returning assets with far less downside than other secondary or co-investment assets in your portfolios. It requires that we re-think how they are put together in portfolios but it also, we believe, requires that they be in portfolios. It is a type of asset that is unlikely to find its way into either your primary or co-investment portfolio.

We will say again, at the risk of boring repetition from prior market overviews: You need to be investing in secondaries, regardless of the current make-up of your portfolio. Not doing so will cause your portfolio to lose out on opportunities that generate superior returns. It really is as simple as that.

Data & Information

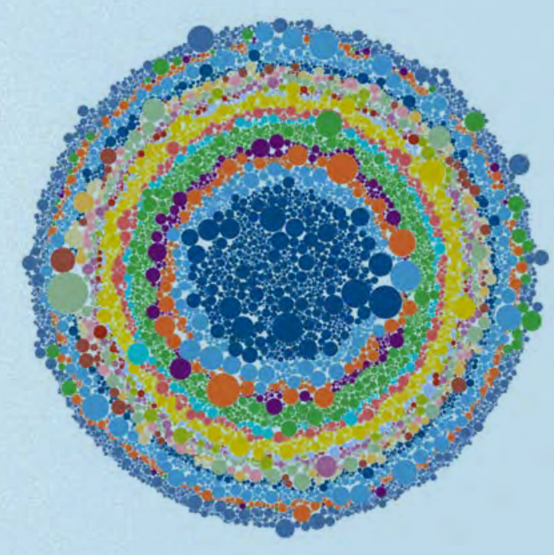
You've gotten this far and, if you have come away with anything, it is probably that Hamilton Lane has a ton of data. We do. We are very proud of that data, which is continually scrubbed ou've gotten this far and, if you have come away with anything, it is probably that Hamilton Lane has a ton of data. We do. We are very proud of that data, which is continually scrubbed for accuracy, and which is as much data aggregated in one place as you'll see anywhere in the private markets.

And our dataset keeps growing every year. But data is only one aspect of gaining a competitive edge. Data alone is not enough. You have to dedicate the time and resources to hire and retain the people and expertise needed to build and develop tools to analyze that data and, ultimately, use it to glean valuable information that helps make better decisions. We'll make this easy by showing a screenshot of the slide we use to give investors a sense of our commitment to this area.

It is full-on, all-in. Want to analyze your existing portfolio? We have you covered. Want to sift through buckets of information to make an informed investment choice? We've got you. Want to look at different market indicators to come up with scenarios and "what-ifs" under different portfolio choices? No problem. Portfolio construction modeling? No one does it better.

The Hamilton Lane
Fund Investment Database

18,500+ Funds | 11,500+ Fund Families*



Source: Hamilton Lane Data (January 2024)

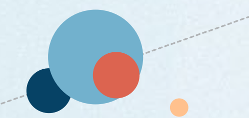
Digital Experience for Today's Private Markets Investor

Striving to deliver transparency and reporting akin to the public markets

Proprietary Technology built by HL

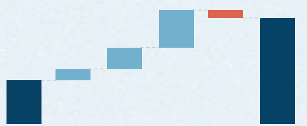
- Designed for HL investment teams and our clients

Portfolio Transparency & Analysis



- Portfolio construction, forecasting and "what-if" analysis
- Custom benchmarking and peer grouping
- Market intelligence: research, data and reports

Digitized Investment Diligence



- Transparency into fund performance and deal metrics
- Expert insights and investment reports, including a view into the HL pipeline

Even a few short years ago, that might have been enough. But the world keeps spinning and technology applications are evolving and improving constantly. AI, blockchain, you name it; it will impact you, us, everyone in the private markets world. In every world. Our industry on the whole may not be ready for it, but we intend to be. We are investing our own money into cutting-edge, private technology companies and applying those technologies to our portfolios, our clients' portfolios and our investment activities. ESG data gathering and monitoring? Talk to Novata. AI analytics application around private markets? Hamilton Lane and TIFIN are bringing you Helix by HL. Passport your way to smooth KYC processes? Call IDR. Think the world will use tokens someday to invest in private markets? So do we, and we're partnering with Securitize to make this happen. Need an easy portal to add private markets exposure to your portfolio? iCapital and CAIS are making that happen globally. The list goes on. In fact, it goes on to 15 companies we've invested in with our balance sheet capital. That's how committed we are to this.

Let us finish this section with a small note about AI. Yes, it will change how we do what we do. Do we know how? We don't, it's still early. We do know, wherever it goes, we will be as cutting edge there as we are in all other aspects of technology. But let's put it in perspective and, for that, let's turn to the words of Joe Walsh, guitarist for the band, The Eagles.

"It's computers, it has nothing to do with music.

It can't destroy a hotel room, it can't throw a TV off the fifth floor into the pool and get it right in the middle.

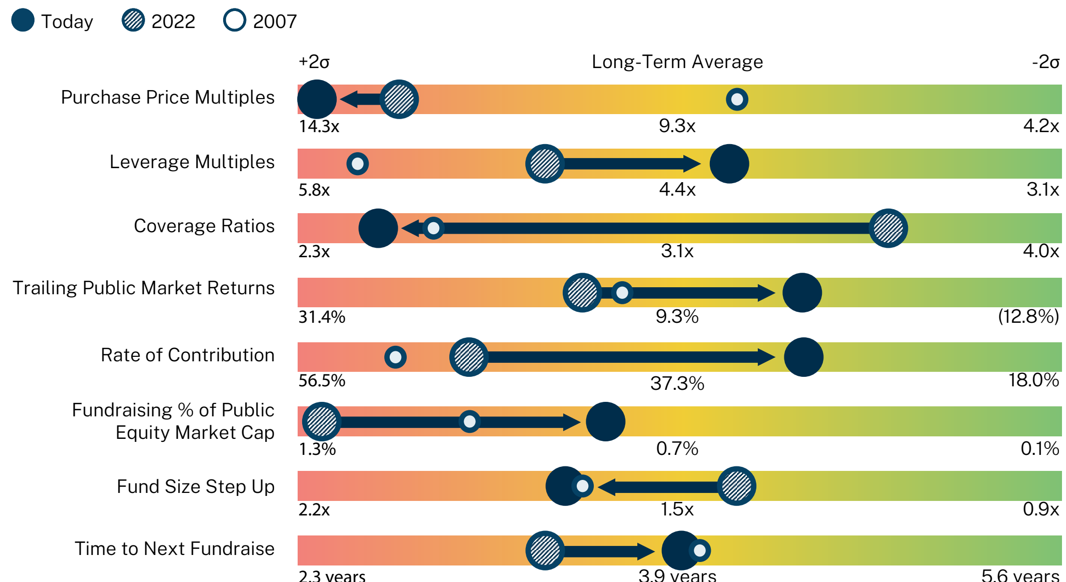
When AI knows how to destroy a hotel room, I'll pay attention to it."

Sentiment Indicators

We're in the home stretch here. And if you made it this far, you've come to one of our favorite sections. We know we have regaled you with stories of derring-do of the private equity managers. How we are calculating and not subject to the emotional pull and tug that afflicts our public equity brethren. It's all a facade. We are as subject to emotion, to swings of fear and greed, as any investor in any area of the investment landscape. We have set about trying to measure that sentiment and see if it can help us identify where we are, or where most investors are, in their market moods.

Let's start with the buyout market.

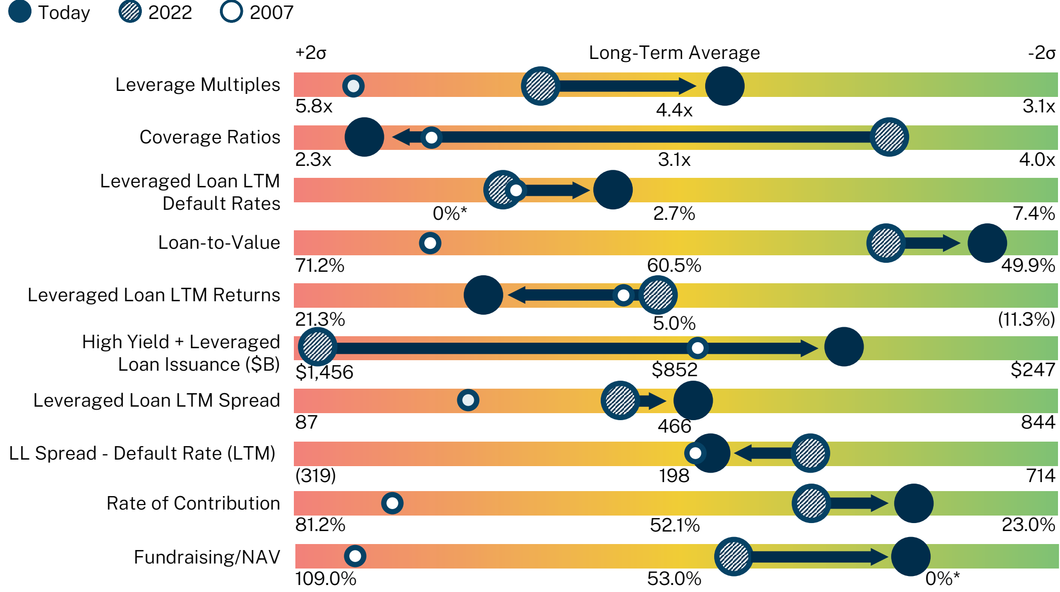
Chart 8.1: Sentiment Indicators: Buyout



Source: Hamilton Lane Data, Bloomberg, Cobalt, Pitchbook, S&P (January 2024)
Note: Values indexed to beginning of year.

Five indicators moved in a positive direction while three moved negative, but overall, we still see it as slightly negative.

Chart 8.2: Sentiment Indicators: Credit

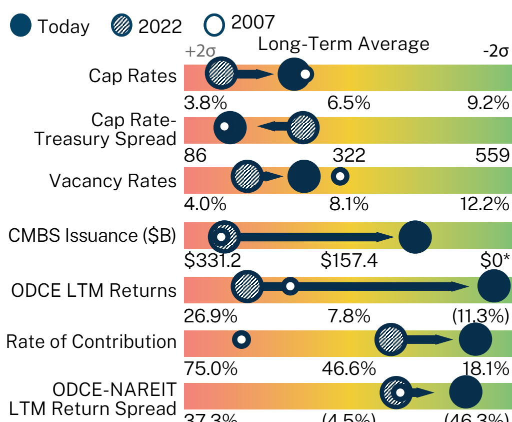


Source: Hamilton Lane Data, Cobalt, Pitchbook, S&P (January 2024)
*Zero used as floor for indicators that cannot be negative
Note: Values indexed to beginning of year.

Not surprisingly, sentiment around the credit market is trending positive and, with higher rates, investors want more exposure to these markets. Watch the coverage ratio carefully, however. It is just one indicator, and you don't want to point to any single thing in this market, but we are looking at that perhaps more than any other today.

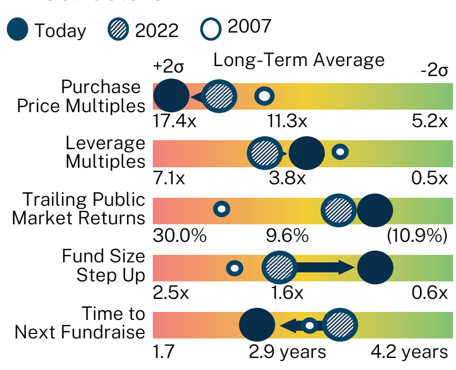
What about real estate and infrastructure?

Chart 8.3: Sentiment Indicators: Real Estate



Source: Hamilton Lane Data, Bloomberg, NCREIF (February 2024)
*Zero used as floor for indicators that cannot be negative
Note: Values indexed to beginning of year.

Chart 8.4: Sentiment Indicators: Infrastructure

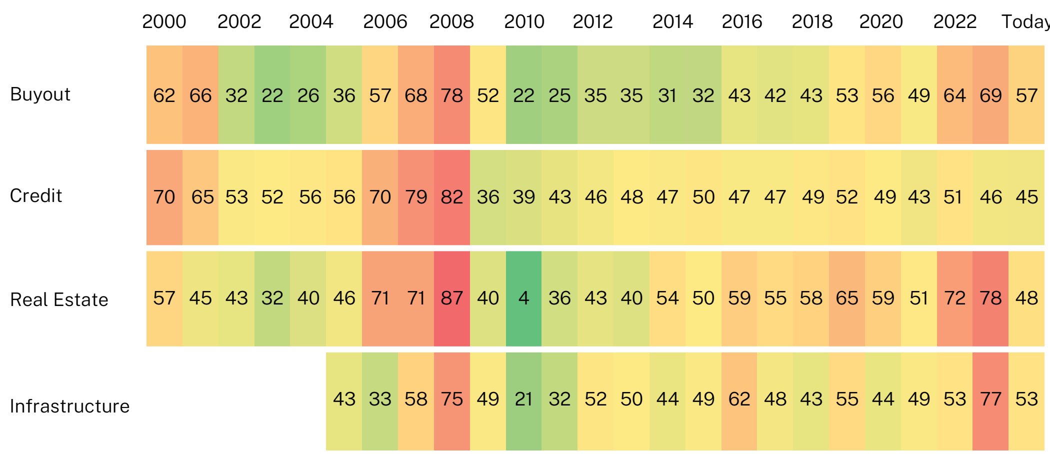


Source: Hamilton Lane Data, Bloomberg, Cobalt, Pitchbook (January 2024)
Note: Values indexed to beginning of year.

Interestingly, both are trending more positive, with real estate significantly more so compared to the prior year's sentiment figures. What's important to note is that on infrastructure, two fairly important indicators – time to next fundraise and purchase price multiples – are trending more negative. They both measure how eager investors are to invest and, right now, they're pretty eager. That's a negative in the sentiment world.

What does it all mean?

Chart 8.5: The Hamilton Lane Worry Index



The Hamilton Lane Worry Index ("HLWI") is a composite view of a wide range of macroeconomic indicators across Buyout, Credit, and Real Assets. Indicators are scaled from 0 to 100 based on their relative value each year, and then averaged to create a market-wide number. Lower numbers represent a generally more favorable environment while high numbers signal a generally less favorable environment. The HLWI is directional and not necessarily indicative of future results.
Source: Hamilton Lane Data, Bloomberg, Cobalt, Pitchbook, S&P, NCREIF (February 2024)

We love our worry index. First, because we call it the worry index. It's a fun name and it also makes us feel like real investors. Most non-investment people would have called it something more positive. Not us. Second, its color-coding makes it really easy to read, which is a big plus for anyone who's made it this far since your eyes are probably burning by now. It tells us that all markets are in a better place than they were last year but that, in general, we remain in firmly neutral territory. That isn't surprising. Sentiment is as indecisive as markets themselves. None of the sub-categories are screaming "buy" or "sell." That's ok. Investors can do quite well in neutral markets.

Conclusion

In all the years penning these overviews, the concluding piece always proves the most challenging to write. How do you conclude after writing thousands of words that, hopefully, all have their own conclusion? If it were so easy to conclude with a summary, why bother with what comes before this? (It's dawning on us in real time that some of you may not have bothered and in fact just skipped to the end... We'll try not to take it too personally.)

Most conclusions have a very bland set of instructions: invest wisely; be careful; diversify. We'll try another way: what not to do or what to do in a slightly more direct way.

Don't avoid hard choices.

Yes, it's an uncertain environment. Yes, there are a million reasons to be cautious and careful and wary. There always are. Stop making excuses for not doing something.

Stop taking the lazy approach to decision making.

Just because someone said so, or you heard that, or you vaguely recalled this, it doesn't make it a good reason to do something (or not do something). The difference between easy and lazy is subtle but, in our experience, you know it when you're guilty of the latter. Don't do it.

Read more. No, not "Hamlet."

(Although, if you are tempted to do that, forget the book – especially after making your way through this opus – and watch Branagh's version instead. It is thorough.) We are often shocked at how little investors read about anything and everything. For example, and not as a recommendation, how much do you know about AI's application to everyday things? Sure, what you heard on the news or what the headline said, but what practitioners in the area are saying? There's a start. What the U.S. Federal Reserve has said about the underlying causes of inflation in the U.S. in 2023? Stuff like that would get the little grey cells humming.

Stop timing the market based on your gut or something you heard.

You know you do that or want to do that. We all do. It's in our nature as investors. We can't help it. But it's like what we are told lousy golf players experience. A series of terrible shots and then one good one that makes them forget all their bad shots and hit another dozen bad ones. You're making this way too hard on yourself. Go find a few good buyout funds, add a dash of venture and growth, a sprinkle of secondary, layer in some solid credit, real estate and infrastructure.

Stop grumbling and complaining.

We are in so many meetings with cries of "this is wrong" and "this is broken" and "this needs to change." Channel your inner MacGyver and go change it or fix it. Don't like that a general partner is taking out a NAV loan? Go sell that fund. Boom. Problem solved. Don't like that fees are too high (or, if you're a general partner, too low)? Go find another place to invest (or, if you're a general partner, another gig). You're in the private markets. You've outperformed your public counterparts for more than 20 years. Think how they feel. You wonder why they doth protest too much? They have good reason – they've been toiling away in the wrong assets for most of their lives.

CONCLUSION

Channel your inner Shakespeare.

Someone once said that good investing is half math and half Shakespeare. (No, not your high school counselor). The basic point is to start spending more time thinking about the psychological and emotional aspects of investing, both yours and of the markets around you. Think we're daft? Let's revisit our theme one last time and borrow a few choice phrases uttered in "Hamlet." (Ok, so really, they're our "Hamlet for Investing Dummies" translations since those are the only books we read). Read them carefully and then tell us if these aren't wise ways to think about investing.

- Listen to many, speak to a few (Yup, listen and learn).
- To thine own self be true (Don't invest in ways that aren't in line with your risk/return philosophy).
- There are more things in heaven and earth, Horatio, than are dreamt of in our philosophy (open your eyes, none of us know what's around the corner or even staring us in the face at times).
- There's nothing either good or bad but thinking makes it so (it's your reaction that matters, not what is happening in the markets; the markets actually don't care about you).

There are more, but you get the gist. You won't be a good investor until, at the very least, you understand your own investment emotions.

Don't settle for anecdotal information.

We'll stop at this one. It makes us nuts how anecdotal private markets can be. It leads to misleading premises and conclusions. Sure, all the data and analysis in the world won't solve good decision making. But no data and analysis will more than likely lead to poorer decision making. Go get the data and fact-based insight you need, then give it a shot.

After that...

Endnotes

Chart 1.4 - MSCI World used as proxy for public equities.

Chart 1.5 - Indices used: Hamilton Lane All Private Markets with volatility de-smoothed; Hamilton Lane All Private Equity ex. Credit and Real Assets with volatility de-smoothed; S&P 500 Index; Russell 3000 Index; MSCI World Index; HFRI Composite Index; Hamilton Lane Private Credit with volatility de-smoothed; Credit Suisse High Yield Index; Barclays Aggregate Bond Index; Hamilton Lane Private Real Estate with volatility de-smoothed; Hamilton Lane Private Infrastructure with volatility de-smoothed; Hamilton Lane Private Natural Resources with volatility de-smoothed; FTSE/NAREIT Equity REIT Index; DJ Brookfield Global Infrastructure Index; MSCI World Energy Sector Index. Geometric mean returns in USD. Assumes risk free rate of 2.4%, representing the average yield of the ten-year treasury over the last fifteen years.

Chart 2.2 - S&P 500 used as a proxy for public equities.

Chart 2.7 - S&P 500 used as proxy for North America public equities, MSCI Europe used as proxy for Western Europe public equities.

Charts 8.1-8.4 - If a data set is distributed normally, about 95% of all data points will lie within two standard deviations of the mean.

Chart 8.5 - The Hamilton Lane Worry Index (“HLWI”) is a composite view of a wide range of macroeconomic indicators across Buyout, Credit, and Real Assets. Indicators are scaled from 0 to 100 based on their relative value each year, and then averaged to create a market-wide number. Lower numbers represent a generally more favorable environment while high numbers signal a generally less favorable environment. The HLWI is directional and not necessarily indicative of future results.

GP Survey - Please be aware that the information contained herein is based upon results of a survey conducted by Hamilton Lane Advisors, L.L.C. (the “Firm”) of a number of private markets participants. The results of the survey may not necessarily represent the opinions of the Firm or its employees, officers or directors. Publication of this report does not indicate an endorsement by the Firm of the results included herein and should not be relied upon when making investment decisions.

Definitions

Desmoothing – A mathematical process to remove serial autocorrelation in the return stream of assets that experience infrequent appraisal pricing, such as private equity. Desmoothed returns may more accurately capture volatility than reported returns. The formula used here for desmoothing is:

Where $rD(t)$ = the desmoothed return for period t,
$r(t)$ = the return for period t, ρ = the autocorrelation

$$rD(t) = (r(t) - r(t-1) * \rho) / (1 - \rho)$$

PME (Public Market Equivalent) – Calculated by taking the fund cash flows and investing them in a relevant index. The fund cash flows are pooled such that capital calls are simulated as index share purchases and distributions as index share sales. Contributions are scaled by a factor such that the ending portfolio balance is equal to the private equity net asset value (equal ending exposures for both portfolios). This seeks to prevent shorting of the public market equivalent portfolio. Distributions are not scaled by this factor. The IRR is calculated based off of these adjusted cash flows.

Sharpe Ratio – The Sharpe Ratio is the average return earned in excess of the risk-free rate per unity of volatility or total risk.

Time-weighted Return – Time-weighted return is a measure of compound rate of growth in a portfolio.

Volatility – Volatility is a statistical measure of dispersion of return, specifically standard deviation.

STRATEGY DEFINITIONS

All Private Markets – Hamilton Lane’s definition of “All Private Markets” includes all private commingled funds excluding fund-of-funds, and secondary fund-of-funds.

Co/Direct Investment Funds – Any PM fund that primarily invests in deals alongside another financial sponsor that is leading the deal.

Continuation Vehicles – A vehicle in which secondary buyers acquire one or more assets from an existing fund.

Corporate Finance/Buyout – Any PM fund that generally takes control position by buying a company.

Credit – This strategy focuses on providing debt capital.

Distressed Debt – Includes any PM fund that primarily invests in the debt of distressed companies.

DM Buyout – Includes any buyout fund that is primarily investing in developed markets of North America, Western Europe and Global

EU Buyout – Any buyout fund primarily investing in the European Union.

Fund-of-Funds (FoF) – A fund that manages a portfolio of investments in other private equity funds.

Growth Equity – Any PM fund that focuses on providing growth capital through an equity investment.

Infrastructure – An investment strategy that invests in physical systems involved in the distribution of people, goods, and resources.

Late Stage VC – A venture capital strategy that provides funding to developed startups.

Mega/Large Buyout – Any buyout fund larger than a certain fund size that depends on the vintage year.

Mezzanine – Includes any PM fund that primarily invests in the mezzanine debt of private companies.

Multi-Stage VC – A venture capital strategy that provides funding to startups across many investment stages.

Natural Resources – An investment strategy that invests in companies involved in the extraction, refinement, or distribution of natural resources.

Origination – Includes any PM fund that focuses primarily on providing debt capital directly to private companies, often using the company's assets as collateral.

Private Equity – A broad term used to describe any fund that offers equity capital to private companies.

Real Assets – Real Assets includes any PM fund with a strategy of Infrastructure, Natural Resources, or Real Estate.

Real Estate – Any closed-end fund that primarily invests in non-core real estate, excluding separate accounts and joint ventures.

ROW – Any fund with a geographic focus outside of North America and Western Europe.

ROW Equity – Includes all buyout, growth, and venture capital-focused funds, with a geographic focus outside of North America and Western Europe.

Secondary FoF – A fund that purchases existing stakes in private equity funds on the secondary market.

Seed/Early VC – A venture capital strategy that provides funding to early-stage startups.

SMID Buyout – Any buyout fund smaller than a certain fund size, dependent on vintage year.

U.S. Mega/Large – Any buyout fund larger than a certain fund size that depends on the vintage year and is primarily investing in the United States.

U.S. SMID – Any buyout fund smaller than a certain fund size that depends on the vintage year and is primarily investing in the United States.

U.S. & EU Growth – Includes all growth equity funds investing in North America and Western Europe.

U.S. & EU VC – Includes all venture capital funds investing in North America and Western Europe.

VC/Growth – Includes all funds with a strategy of venture capital or growth equity.

Venture Capital – Venture Capital incudes any PM fund focused on financing startups, early-stage, late stage, and emerging companies or a combination of multiple investment stages of startups.

INDEX DEFINITIONS

Barclays U.S. Corporate Aggregate Index – Tracks the performance of U.S. fixed rate corporate debt rated as investment grade.

BofAML High Yield Index – The BofAML High Yield index tracks the performance of below investment grade U.S. dollar-denominated corporate bonds publicly issued in the U.S. domestic market.

Credit Suisse High Yield Index – The Credit Suisse High Yield index tracks the performance of U.S. sub-investment grade bonds.

Credit Suisse Leveraged Loan Index – The CS Leveraged Loan Index represents tradable, senior-secured, U.S. dollar-denominated non-investment grade loans.

DJ Brookfield Global Infrastructure Index – The DJ Brookfield Global Infrastructure Index is designed to measure the performance of companies globally that are operators of pure-play infrastructure assets.

FTSE/NAREIR All Equity REIT Index – The FTSE/NAREIT All Equity REIT Index tracks the performance of U.S. equity REITs.

HFRI Composite Index – The HFRI Composite Index reflects hedge fund industry performance.

MSCI Europe Index – The MSCI Europe Index measures performance of large and mid-cap companies across 15 developed markets in Europe.

MSCI USA Small Cap Value Index – The MSCI USA Small Cap Index is designed to measure the performance of the small cap segment of the U.S. equity market.

MSCI World Energy Sector Index – The MSCI World Energy Sector Index measures the performance of securities classified in the GICS Energy sector.

MSCI World Index – The MSCI World Index tracks large and mid-cap equity performance in developed market countries.

Russell 1000 Index – The Russell 1000 Index tracks the highest-ranking 1000 stocks in the Russell 3000 index by market capitalization

Russell 2000 Index – The Russell 2000 Index is composed of 20000 small-cap U.S. companies.

Russell 3000 Index – The Russell 3000 Index is composed of 3000 large U.S. companies, as determined by market capitalization.

S&P 500 Index – The S&P 500 Index tracks 500 largest companies based on market capitalization of companies listed on NYSE or NASDAQ.

S&P 600 Index – The S&P 600 Index tracks small-cap companies in the U.S. based on market capitalization

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