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How Private Equity Has Weathered the Storm of COVID-19

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Few industries can say they had a record year in 2020, but the private equity sector boasts just that. Though the shocking onslaught of COVID-19 took its toll in the second quarter, PE weathered the storm and ended the year strong in a stunning show of resiliency and agility.

It’s not altogether surprising. Historically, PE investments in global downturns demonstrate higher returns than those made during normal markets. 2020 is still in sight in the rearview, but by all indications, it was no exception to this trend. The future looks highly optimistic for PE firms across the globe—and in fact, it’s likely they’ll be instrumental in continued economic recovery.

What the Numbers Tell Us About PE in 2020

PE had its share of COVID-related pain. According to Bain & Company, the total number of deals throughout 2020 was down a massive 25% from recent norms—short around 1,000 deals. Incredibly, though, the year ended on a high note, with deal value—primarily from the 3rd and 4th quarters—generating $592 billion; 8% higher than 2019.

Together, these numbers indicate that 2020 deals were much larger in value than the average investment. This also helps explain why, despite the number of exits trailing those of 2019, global exit value remained on par with recent years.

Interestingly, 2020 also saw a big spike in the number and impact of SPACs, a trend that PE firms are increasingly leveraging. Smashing previous records by 600%, SPACs raised $83 billion in new capital in 2020—and continues the pace with $50 billion raised in 2021 through February alone. McKinsey notes that of the 111 US IPOs in the first 8 months of 2020, SPACs accounted for 81 of them.

Industries driving these record PE numbers were those that found themselves thriving in the pandemic environment, particularly in the technology sector. In fact, IT deals increased by a massive 72.4% from 2019, while tech fundraising in the U.S. surpassed every prior record. Unsurprisingly, healthcare is another sector ripe for PE, with significant year-over-year growth in investment volume.

Looking at the Future of Private Equity Post-Covid

PE firms around the globe exited 2020 with almost $1.5 trillion of dry powder, setting the stage for formidable growth ahead. A Deloitte forecasting model predicts global PE AUM to rise substantially over the next four years, with a potentially unrealized value of $6 trillion over an AUM of $4.5T in 2019.

IT and healthcare will continue to drive PE opportunities in coming months and years. The consumer, industrial, and financial sectors are also in the top five for PE focus in the next 12 months, but there has been a declining interest in these three areas compared to previous years.

Regardless of industry, one pivotal role PE firms have had throughout the pandemic is their support of portfolio companies, particularly smaller ones. Whether this is in the form of fresh investments and debt refinancing or expertise in cash flow management, operational best practices, or recovery plans, PE firms are there to ensure success and, most importantly, generate returns. Deloitte reports that portfolio companies with less than $100M appeared particularly grateful for this support, steering them through the crisis and protecting them from risk and negative outcomes. This is key positioning for the sector moving forward post-COVID.

Another critical PE trend going into 2021 and beyond is diversity. Against a competitive landscape, many firms are recognizing the need to stand out in order to build relationships and win deals—one of the ways they are choosing to differentiate is through a more diverse team. Adding board members and team members who have diverse backgrounds and experiences are likely to resonate better with potential portfolio companies that prioritize diversity.

This topic of diversity dovetails into the larger conversation of ESG within the PE sector. This is an area where PE firms have received skepticism in the past. A recent survey published by Ernst & Young revealed that only 24% of PE firms seriously considered environmental, social, and governance matters in the deal evaluation process. Larger firms, with more than $15 billion in assets, are more likely to prioritize ESG than smaller firms, but asset growth and talent always take priority. That said, the number of firms who are beginning to introduce ESG into their strategies is slowly increasing, and it seems as if the pandemic only advanced that momentum. In fact, ESG-related regulations are already hitting Europe, and the US will likely respond accordingly.

A Positive Outlook for the PE Sector

Ultimately, it's clear that private equity firms have held onto strong roots to fare the worst of COVID-19. Their impressive returns and supportive efforts have played no small part in economic recovery across the globe. As we look ahead to widespread vaccine-rollout and a "new normal" in the business world, PE firms will continue to adapt and evolve, taking on new challenges with matured perspectives and innovative strategies.